

PRESCOTT v. JONES

69 N.H. 305, 41 A. 352 (1898)

Assumpsit. The declaration alleged, in substance, that the defendants, as insurance agents, had insured the plaintiff's buildings in the Manchester Fire Insurance Company until February 1, 1897; that on January 23, 1897, they notified him that they would renew the policy and insure his

60. The duty to take positive action will be taken up again when we deal with insurance contracts in Ch. 4, §3.

buildings for a further term of one year from February 1, 1897, in the sum of \$500, unless notified to the contrary by him; that he, relying on the promise to insure unless notified to the contrary, and believing, as he had a right to believe, that the buildings would be insured by the defendants for one year from February 1, 1897, gave no notice to them to insure or not to insure; that they did not insure the buildings as they had agreed and did not notify him of their intention not to do so; that the buildings were destroyed by fire March 1, 1897, without fault on the plaintiff's part. The defendants demurred.

BLODGETT, J. While an offer will not mature into a complete and effectual contract until it is acceded to by the party to whom it is made and notice thereof, either actual or constructive, given to the maker (*Abbott v. Shepard*, 48 N.H. 14, 17; *Perry v. Insurance Co.*, 67 N.H. 291, 294, 295), it must be conceded to be within the power of the maker to prescribe a particular form or mode of acceptance; and the defendants having designated in their offer what they would recognize as notice of its acceptance, namely, failure of the plaintiff to notify them to the contrary, they may properly be held to have waived the necessity of formally communicating to them the fact of its acceptance by him.

But this did not render acceptance on his part any less necessary than it would have been if no particular form of acceptance had been prescribed, for it is well settled that "a party cannot, by the wording of his offer, turn the absence of communication of acceptance into an acceptance, and compel the recipient of his offer to refuse it at the peril of being held to have accepted it." *Clark Cont.* 31, 32. "A person is under no obligation to do or say anything concerning a proposition which he does not choose to accept. There must be actual acceptance or there is no contract." *More v. Insurance Co.*, 130 N.Y. 537, 547. And to constitute acceptance, "there must be words, written or spoken, or some other overt act." *Bish. Cont.*, s. 329, and authorities cited.

If, therefore, the defendants might and did make their offer in such a way as to dispense with the communication of its acceptance to them in a formal and direct manner, they did not and could not so frame it as to render the plaintiff liable as having accepted it merely because he did not communicate his intention not to accept it. And if the plaintiff was not bound by the offer until he accepted it, the defendants could not be, because "it takes two to make a bargain," and as contracts rest on mutual promises, both parties are bound, or neither is bound.

The inquiry as to the defendants' liability for the non-performance of their offer thus becomes restricted to the question, Did the plaintiff accept the offer, so that it became by his action clothed with legal consideration and perfected with the requisite condition of mutuality? As, in morals, one who creates an expectation in another by a gratuitous promise is doubtless bound to make the expectation good, it is perhaps to be regretted that, upon the facts before us, we are constrained to answer the

questions in the negative. While a gratuitous undertaking is binding in honor, it does not create a legal responsibility. Whether wisely or equitably or not, the law requires a consideration for those promises which it will enforce; and as the plaintiff paid no premium for the policy which the defendants proposed to issue, nor bound himself to pay any, there was no legal consideration for their promise, and the law will not enforce it.

Then, again, there was no mutuality between the parties. All the plaintiff did was merely to determine in his own mind that he would accept the offer — for there was nothing whatever to indicate it by way of speech or other appropriate act. Plainly, this did not create any rights in his favor as against the defendants. From the very nature of a contract this must be so; and it therefore seems superfluous to add that the universal doctrine is that an uncommunicated mental determination cannot create a binding contract.

Nor is there any estoppel against the defendants, on the ground that the plaintiff relied upon their letter and believed they would insure his buildings as therein stated.

The letter was a representation only of a present intention or purpose on their part.

It was not a statement of a fact or state of things actually existing, or past and executed, on which a party might reasonably rely as fixed and certain, and by which he might properly be guided in his conduct. . . . The intent of a party, however positive or fixed, concerning his future action, is necessarily uncertain as to its fulfillment, and must depend on contingencies and be subject to be changed and modified by subsequent events and circumstances. . . . On a representation concerning such a matter no person would have a right to rely, or to regulate his action in relation to any subject in which his interest was involved as upon a fixed, certain, and definite fact or state of things, permanent in its nature and not liable to change. . . . The doctrine of estoppel . . . on the ground that it is contrary to a previous statement of a party does not apply to such a representation. The reason on which the doctrine rests is, that it would operate as a fraud if a party was allowed to aver and prove a fact to be contrary to that which he had previously stated to another for the purpose of inducing him to act and to alter his condition, to his prejudice, on the faith of such previous statement. But the reason wholly fails when the representation relates only to a present intention or purpose of a party, because, being in its nature uncertain and liable to change, it could not properly form a basis or inducement upon which a party could reasonably adopt any fixed and permanent course of action.

Langdon v. Doud, 10 Allen 433, 436, 437; Jackson v. Allen, 120 Mass. 64, 79; Jorden v. Money, 5 H.L. Cas. 185.

“An estoppel cannot arise from a promise as to future action with respect to a right to be acquired upon an agreement not yet made.” Insurance Co. v. Mowry, 96 U.S. 544, 547. “The doctrine has no place

for application when the statement relates to rights depending upon contracts yet to be made, to which the person complaining is to be a party. He has it in his power in such cases to guard in advance against any consequences of a subsequent change of intention by the person with whom he is dealing.” *Ib.* 548. . . .

To sum it up in a few words, the case presented is, in its legal aspects, one of a party seeking to reap where he had not sown, and to gather where he had not scattered.

Demurrer sustained.

NOTE

Same decision today under §69 of Restatement Second? Is the distinction between promissory estoppel and estoppel in pais still adhered to? See the discussion in *Feinberg v. Pfeiffer Co.*, *infra* p. 308.

The holder of a fire policy that has just expired claims that under a local custom fire policies are automatically renewed unless cancelled by either party. Relevant? *City Mortgage & Discount Company v. Palatine Insurance Company*, 226 Ala. 179, 145 So. 490 (1933); Restatement Second §§219-223.

CARLILL v. CARBOLIC SMOKE BALL CO.

[1893] 1 Q.B. 256 (C.A. 1892)

Appeal from a decision of Hawkins, J. [1892] 2 Q.B. 484.

The defendants, who were the proprietors and vendors of a medical preparation called "The Carbolic Smoke Ball," inserted in the Pall Mall

132. Restatement Second §12, Reporter's Note (Tent. Draft No. 1, 1964):

As defined in the original Restatement, "unilateral contract" included three quite different types of transaction: (1) the promise which does not contemplate a bargain, such as the promise under seal to make a gift, (2) certain option contracts, such as the option under seal (see §§24A, 45), and (3) the bargain completed on one side, such as the loan which is to be repaid. This grouping of unlike transactions was productive of confusion.

133. See also §30. It reads:

Form of Acceptance Invited

(1) An offer may invite or require acceptance to be made by an affirmative answer in words, or by performing or refraining from performing a specified act, or may empower the offeree to make a selection of terms in this acceptance.

(2) Unless otherwise indicated by the language or the circumstances, an offer invites acceptance in any manner and by any medium reasonable in the circumstances.

[See also §55].

134. It reads:

Option Contract Created by Part Performance or Tender

(1) Where an offer invites an offeree to accept by rendering a performance and does not invite a promissory acceptance, an option contract is created when the offeree begins the invited performance or tenders part of it.

(2) The offeror's duty of performance under any option contract so created is conditional on completion or tender of the invited performance in accordance with the terms of the offer.

Consult also, §25; §87, *supra* p. 315.

Gazette of November 13, 1891, and in other newspapers, the following advertisement:

£100 reward will be paid by the Carbolic Smoke Ball Company to any person who contracts the increasing epidemic influenza, colds, or any disease caused by taking cold, after having used the ball three times daily for two weeks according to the printed directions supplied with each ball. £1000 is deposited with the Alliance Bank, Regent Street shewing our sincerity in the matter.

During the last epidemic of influenza many thousand carbolic smoke balls were sold as preventives against this disease, and in no ascertained case was the disease contracted by those using the carbolic smoke ball.

One carbolic smoke ball will last a family several months, making it the cheapest remedy in the world at the price, 10s., post free. The ball can be refilled at a cost of 5s. Address, Carbolic Smoke Ball Company, 27 Princes Street, Hanover Square, London.

The plaintiff, a lady, on the faith of this advertisement, bought one of the balls at a chemist's and used it as directed, three times a day, from November 20, 1891, to January 17, 1892, when she was attacked by influenza. Hawkins, J., held that she was entitled to recover the £100. The defendants appealed.

LINDLEY, L.J. . . . We must first consider whether this was intended to be a promise at all, or whether it was a mere puff which meant nothing. Was it a mere puff? My answer to that question is "No," and I base my answer upon this passage: "£1000 is deposited with the Alliance Bank, shewing our sincerity in the matter." Now, for what was that money deposited or that statement made except to negative the suggestion that this was a mere puff and meant nothing at all? The deposit is called in aid by the advertiser as a proof of his sincerity in the matter — that is, the sincerity of his promise to pay this £100 in the event which he has specified. I say this for the purpose of giving point to the observation that we are not inferring a promise; there is the promise, as plain as words can make it.

Then it is contended that it is not binding. In the first place, it is said that it is not made with anybody in particular. Now that point is common to the words of this advertisement and to the words of all other advertisements offering rewards. They are offers to anybody who performs the conditions named in the advertisement, and anybody who does perform the conditions accepts the offer. In point of law this advertisement is an offer to pay £100 to anybody who will perform these conditions, and the performance of the conditions, is the acceptance of the offer. That rests upon a string of authorities, the earliest of which is *Williams v. Carwardine*, 4 Barn. & Adol. 621, which has been followed by many other decisions upon advertisements offering rewards.

But then it is said, "Supposing that the performance of the conditions is an acceptance of the offer, that acceptance ought to have been notified." Unquestionably, as a general proposition, when an offer is made, it is necessary in order to make a binding contract, not only that it should be accepted, but that the acceptance should be notified. But is that so in cases of this kind? I apprehend that they are an exception to that rule, or, if not an exception, they are open to the observation that the notification of the acceptance need not precede the performance. This offer is a continuing offer. It was never revoked, and if notice of acceptance is required — which I doubt very much, for I rather think the true view is that which was expressed and explained by Lord Blackburn in the case of *Brogden v. Railway Co.*, 2 App. Cas. 666, 691, — if notice of acceptance is required, the person who makes the offer gets the notice of acceptance contemporaneously with his notice of the performance of the condition. If he gets notice of the acceptance before his offer is revoked, that in principle is all you want. I, however, think that the true view, in a case of this kind, is that the person who makes the offer shows by his language and from the nature of the transaction that he does not expect and does not require notice of the acceptance apart from notice of the performance. . . .

I come now to the last point which I think requires attention: that is, the consideration. It has been argued that this is *nudum pactum* — that there is no consideration. We must apply to that argument the usual legal tests. Let us see whether there is no advantage to the defendants. It is said that the use of the ball is no advantage to them, and that what benefits them is the sale; and the case is put that a lot of these balls might be stolen, and that it would be no advantage to the defendants if the thief or other people used them. The answer to that, I think, is as follows: It is quite obvious that in view of the advertisers a use by the public of their remedy, if they can only get the public to have confidence enough to use it, will react and produce a sale which is directly beneficial to them. Therefore, the advertisers get out of the use an advantage which is enough to constitute a consideration.

But there is another view. Does not the person who acts upon this advertisement and accepts the offer put himself to some inconvenience at the request of the defendants? Is it nothing to use this ball three times daily for two weeks according to the directions at the request of the advertiser? Is that to go for nothing? It appears to me that there is a distinct inconvenience, not to say a detriment, to any person who so uses the smoke ball. I am of opinion, therefore, that there is ample consideration for the promise. . . .

BOWEN, L.J. . . . Then it was said that there was no notification of the acceptance of the contract. One cannot doubt that, as an ordinary rule of law, an acceptance of an offer made ought to be notified to the person

who makes the offer, in order that the two minds may come together. Unless this is done, the two minds may be apart, and there is not that consensus which is necessary according to the English law — I say nothing about the laws of other countries — to make a contract. But there is this clear gloss to be made upon that doctrine, that as notification of acceptance is required for the benefit of the person who makes the offer, the person who makes the offer may dispense with notice to himself if he thinks it desirable to do so, and I suppose there can be no doubt that where a person in an offer made by him to another person, expressly or impliedly intimates a particular mode of acceptance as sufficient to make the bargain binding, it is only necessary for the other person to whom such offer is made to follow the indicated method of acceptance; and if the person making the offer, expressly or impliedly intimates in his offer that it will be sufficient to act on the proposal without communicating acceptance of it to himself, performance of the condition is a sufficient acceptance without notification.

That seems to me to be the principle which lies at the bottom of the acceptance cases, of which two instances are the well-known judgment of Mellish, L.J., in *Harris's Case*, L.R. 7 Ch. 587, and the very instructive judgment of Lord Blackburn in *Brogden v. Railway Co.*, 2 App. Cas. 666, 691, in which he appears to me to take exactly the line I have indicated.

Now, if that is the law, how are we to find out whether the person who makes the offer does intimate that notification of acceptance will not be necessary in order to constitute a binding bargain? In many cases you look to the offer itself. In many cases you extract from the character of the transaction that notification is not required, and in the advertisement cases it seems to me to follow as an inference to be drawn from the transaction itself that a person is not to notify his acceptance of the offer before he performs the condition, but that if he performs the condition notification is dispensed with. It seems to me that from the point of view of common sense no other idea could be entertained. If I advertise to the world that my dog is lost, and that anybody who brings the dog to a particular place will be paid some money, are all the police or other persons whose business it is to find lost dogs to be expected to sit down and write a note saying that they have accepted my proposal? Why, of course, they at once look after the dog, and as soon as they find the dog they have performed the condition. The essence of the transaction is that the dog should be found, and it is not necessary under such circumstances, as it seems to me, that in order to make the contract binding there should be any notification of acceptance. It follows from the nature of the thing that the performance of the condition is sufficient acceptance without the notification of it, and a person who makes an offer in an advertisement of that kind makes an offer which must be read by the light of that common sense reflection. He does, therefore, in his offer

impliedly indicate that he does not require notification of the acceptance of the offer.

Appeal dismissed.

DICKINSON v. DODDS

2 Ch. D. 463 (C.A. 1876)

On Wednesday, the 10th of June, 1874, the Defendant John Dodds signed and delivered to the Plaintiff, George Dickinson, a memorandum, of which the material part was as follows:

I hereby agree to sell to Mr. George Dickinson the whole of the dwelling-houses, garden ground, stabling, and outbuildings thereto belonging, situate at Croft, belonging to me, for the sum of £800. As witness my hand this tenth day of June, 1874.

£800

(Signed) JOHN DODDS.

P.S. — This offer to be left over until Friday, 9 o'clock, A.M. J.D. (the twelfth), 12th June, 1874.¹¹⁷

(Signed) J. DODDS.

. . . In the afternoon of the Thursday the Plaintiff was informed by a Mr. Berry that Dodds had been offering or agreeing to sell the property to Thomas Allan, the other Defendant. Thereupon the Plaintiff, at about half-past seven in the evening, went to the house of Mrs. Burgess, the mother-in-law of Dodds, where he was then staying, and left with her a formal acceptance in writing of the offer to sell the property. According to the evidence of Mrs. Burgess this document never in fact reached Dodds, she having forgotten to give it to him.

On the following (Friday) morning, at about seven o'clock, Berry, who was acting as agent for Dickinson, found Dodds at the Darlington railway station, and handed to him a duplicate of the acceptance by Dickinson, and explained to Dodds its purport. He replied that it was too late, as he had sold the property. A few minutes later Dickinson himself found Dodds entering a railway carriage, and handed him another duplicate of the notice of acceptance, but Dodds declined to receive it, saying, "You are too late. I have sold the property."

¹¹⁷. Could Dodds, intending to keep the property, prevent timely acceptance by being unavailable till the 13th? Absent timely revocation, could Dickinson still accept on that day? 1 Corbin §35. — EDS.

It appeared that on the day before, Thursday, the 11th of June, Dodds had signed a formal contract for the sale of the property to the Defendant Allan for £800, and had received from him a deposit of £40.

The bill in this suit prayed that the Defendant Dodds might be decreed specifically to perform the contract of the 10th of June, 1874; that he might be restrained from conveying the property to Allan; that Allan might be restrained from taking any such conveyance; that, if any such conveyance had been or should be made, Allan might be declared a trustee of the property for, and might be directed to convey the property to, the Plaintiff; and for damages.

The cause came on for hearing before Vice-Chancellor Bacon on the 25th of January, 1876.

[BACON, V.C., decreed specific performance, holding that Dodds could withdraw only by giving notice to Dickinson and that owing to the relation back of the acceptance to the date of the agreement, the property in equity was the property of plaintiff and Dodds had nothing to sell to Allan.]

From this decision both the defendants appeal. . . .

MELLISH, L.J. . . . The first question is, whether this document of the 10th of June, 1874, which was signed by Dodds, was an agreement to sell, or only an offer to sell, the property therein mentioned to Dickinson; and I am clearly of opinion that it was only an offer, although it is in the first part of it, independently of the postscript, worded as an agreement. I apprehend that, until acceptance, so that both parties are bound, even though an instrument is so worded as to express that both parties agreed, it is in point of law only an offer, and until both parties are bound, neither party is bound. It is not necessary that both parties should be bound within the Statute of Frauds, for, if one party makes an offer in writing, and the other accepts it verbally, that will be sufficient to bind the person who has signed the written document. But, if there be no agreement, either verbally or in writing, then, until acceptance, it is in point of law an offer only, although worded as if it were an agreement. But it is hardly necessary to resort to that doctrine in the present case, because the postscript calls it an offer, and says, "This offer to be left over until Friday, 9 o'clock A.M." Well, then, this being only an offer, the law says — and it is a perfectly clear rule of law — that, although it is said that the offer is to be left open until Friday morning at 9 o'clock, that did not bind Dodds. He was not in point of law bound to hold the offer over until 9 o'clock on Friday morning. He was not so bound either in law or in equity. Well, that being so, when on the next day he made an agreement with Allan to sell the property to him, I am not aware of any ground on which it can be said that that contract with Allan was not as good and binding a contract as ever was made. Assuming Allan to have known (there is some dispute about it, and Allan does not admit that he knew of it, but I will assume that he did) that Dodds had made the offer to

Dickinson, and had given him till Friday morning at 9 o'clock to accept it, still in point of law that could not prevent Allan from making a more favourable offer than Dickinson, and entering at once into a binding agreement with Dodds.

Then Dickinson is informed by Berry that the property has been sold by Dodds to Allan. Berry does not tell us from whom he heard it, but says that he did hear it, that he knew it, and that he informed Dickinson of it. Now, stopping there, the question which arises is this — If an offer has been made for the sale of property, and before that offer is accepted, the person who has made the offer enters into a binding agreement to sell the property to somebody else, and the person to whom the offer was first made receives notice in some way that the property has been sold to another person, can he after that make a binding contract by the acceptance of the offer? I am of opinion that he cannot. The law may be right or wrong in saying that a person who has given to another a certain time within which to accept an offer is not bound by his promise to give that time; but, if he is not bound by that promise, and may still sell the property to some one else, and if it be the law that, in order to make a contract, the two minds must be in agreement at some one time, that is, at the time of the acceptance, how is it possible that when the person to whom the offer has been made knows that the person who has made the offer has sold the property to someone else, and that, in fact, he has not remained in the same mind to sell it to him, he can be at liberty to accept the offer and thereby make a binding contract? It seems to me that would be simply absurd. If a man makes an offer to sell a particular horse in his stable, and says, "I will give you until the day after to-morrow to accept the offer," and the next day goes and sells the horse to somebody else, and receives the purchase-money from him, can the person to whom the offer was originally made then come and say, "I accept," so as to make a binding contract, and so as to be entitled to recover damages for the non-delivery of the horse? If the rule of law is that a mere offer to sell property, which can be withdrawn at any time, and which is made dependent on the acceptance of the person to whom it is made, is a mere nudum pactum, how is it possible that the person to whom the offer has been made can by acceptance make a binding contract after he knows that the person who has made the offer has sold the property to some one else? It is admitted law that, if a man who makes an offer dies, the offer cannot be accepted after he is dead, and parting with the property has very much the same effect as the death of the owner, for it makes the performance of the offer impossible. I am clearly of opinion that, just as when a man who has made an offer dies before it is accepted it is impossible that it can then be accepted, so when once the person to whom the offer was made knows that the property has been sold to some one else, it is too late for him to accept the offer, and on that ground I am clearly of opinion that there

was no binding contract for the sale of this property by Dodds to Dickinson, and even if there had been, it seems to me that the sale of the property to Allan was first in point of time. However, it is not necessary to consider, if there had been two binding contracts, which of them would be entitled to priority in equity, because there is no binding contract between Dodds and Dickinson.

BAGGALLAY, J.A. I entirely concur in the judgments which have been pronounced.

JAMES, L.J. The bill will be dismissed with costs.

[The concurring opinion of James, L.J. has been omitted.]

NOTE

1. Professor Winfield, in criticizing the decision as unsound, makes the following point in *Pollock's Principles of Contract* 21 (13th ed. 1950):

A [Dodds] stated in his offer the exact price of the house. That was the consideration on his side. Why should the law insist that he was entitled to extra consideration for allowing the offeree a certain time within which he could accept? Presumably he might have taken that very factor into account in fixing the sum that constituted the price, i.e., he may have fixed it rather higher than he would have done if no time had been specified.

See also State of New York, Law Revision Commission 57 (2d Annual Report, 1936). Suppose Dodds before acceding to the postscript had raised the price to £805. Different result? Is not the increased chance of an acceptance on the part of the offeree or the likelihood of reliance by the offeree sufficient consideration? For an interesting explanation of *Dickinson v. Dodds* in terms of the philosophy of contracts of the time, see J. Dawson, W. Harvey & S. Henderson, *Cases and Comment on Contracts* 335, 336 (4th ed. 1982). Consult *Maughs v. Porter*, 157 Va. 415, 161 S.E. 242 (1931); *Boston & Maine R.R. v. Bartlett*, 57 Mass. (3 Cush.) 224 (1849). Was it of any significance that the postscript contained the word "over" instead of "open"? Is either word free from ambiguity? See *The New York Statute on Irrevocable Offers*, 43 Colum. L. Rev. 487, 488-490 (1943); 46 Mich. L. Rev. 58, 60 (1947).

2. Suppose plaintiff, relying on the offer, had spent £5 to have the title searched. Should he be entitled to get specific performance, or at least to get a refund? *Bard v. Kent*, 19 Cal. 2d 449, 122 P.2d 8, 139 A.L.R. 1032 (1942).

3. Was it irrelevant that the defendant's promise was in writing?

4. Has the "naked" promise to keep an offer open for a certain period any legal significance? Suppose on Thursday plaintiff had offered £750

and the defendant had remained silent. Could plaintiff still accept on Friday, assuming that the property had not been sold in the meantime? Restatement Second §39. Assume that the defendant replied, "Must insist on £800"; can plaintiff accept? Consult *Livingstone v. Evans*, [1954] 4 D.L.R. (Alta. Sup. Ct.).

5. Suppose Dodds had sold the property but without plaintiff's knowledge. Same result? *Threlkeld v. Inglett*, 289 Ill. 90, 124 N.E. 368 (1919). Is it relevant whether Berry was authorized by Dodds to convey the information, and whether Dickinson could regard the information as reliable? Restatement second §43.

6. Why did the notice of acceptance left by plaintiff with Mrs. Burgess not complete the contract? Restatement Second §68.

7. The rule in *Dickinson v. Dodds* has been one of the main targets of the critics of the consideration doctrine. "It may . . . be ordinary business understanding that an offer for a bargain is revocable until the bargain is made, and to that extent, our common law is sound. To say, however, that a firm offer will not be given effect according to its terms, is something quite different." Sharp, *Promissory Liability* (pt. 1), 7 U. Chi. L. Rev. 10 (1939). The Sixth Interim Report of the English Law Revision Commission (1937) has expressed itself (p. 22) in favor of making the firm offer irrevocable even if orally made, provided it contains a definite time limit. Statutory changes enacted in New York since 1941 require a writing to dispense with consideration. See p. 549 *infra*. For the English law, see G. H. Treitel, *The Law of Contract* 99-100 (5th ed. 1974). In the case of international sales of goods, the rule has been expressly abolished by legislation. ULFIS Art. 5(2). See Farnsworth, *Mutuality of Obligation in Contract Law*, 3 Dayton L. Rev. 271 (1978).

JAMES BAIRD CO. v. GIMBEL BROS.

64 F.2d 344 (2d Cir. 1933)

L. HAND, Circuit Judge. The plaintiff sued the defendant for breach of a contract to deliver linoleum under a contract of sale; the defendant denied the making of the contract; the parties tried the case to the judge under a written stipulation and he directed judgment for the defendant. The facts as found, bearing on the making of the contract, the only issue necessary to discuss, were as follows: The defendant, a New York merchant, knew that the Department of Highways in Pennsylvania had asked for bids for the construction of a public building. It sent an employee to the office of a contractor in Philadelphia, who had possession of the specifications, and the employee there computed the amount of the linoleum which would be required on the job, underestimating the total yardage by about one-half the proper amount. In ignorance of this mistake, on December twenty-fourth the defendant sent to some twenty or thirty contractors, likely to bid on the job, an offer to supply all linoleum required by the specifications at two different lump sums, depending upon the quality used. These offers concluded as follows: "If successful in being awarded this contract, it will be absolutely guaranteed, . . . and . . . we are offering these prices for reasonable" (sic), "prompt acceptance after the general contract has been awarded." The plaintiff, a contractor in Washington, got one of these on the twenty-eighth, and on the same day the defendant learned its mistake and telegraphed all the contractors to whom it had sent the offer, that it withdrew it and would substitute a new one at about double the amount of the old. This with-

drawal reached the plaintiff at Washington on the afternoon of the same day but not until after it had put in a bid at Harrisburg at a lump sum, based as to linoleum upon the prices quoted by the defendant. The public authorities accepted the plaintiff's bid on December thirtieth, the defendant having meanwhile written a letter of confirmation of its withdrawal, received on the thirty-first. The plaintiff formally accepted the offer on January second, and, as the defendant persisted in declining to recognize the existence of a contract, sued it for damages on a breach.

Unless there are circumstances to take it out of the ordinary doctrine, since the offer was withdrawn before it was accepted, the acceptance was too late. Restatement of Contracts, §35. To meet this the plaintiff argues as follows: It was a reasonable implication from the defendant's offer that it should be irrevocable in case the plaintiff acted upon it, that is to say, used the prices quoted in making its bid, thus putting itself in a position from which it could not withdraw without great loss. While it might have withdrawn its bid after receiving the revocation, the time had passed to submit another, and as the item of linoleum was a very trifling part of the cost of the whole building, it would have been an unreasonable hardship to expect it to lose the contract on that account, and probably forfeit its deposit. While it is true that the plaintiff might in advance have secured a contract conditional upon the success of its bid, this was not what the defendant suggested. It understood that the contractors would use its offer in their bids, and would thus in fact commit themselves to supplying the linoleum at the proposed prices. The inevitable implication from all this was that when the contractors acted upon it, they accepted the offer and promised to pay for the linoleum, in case their bid were accepted.

It was of course possible for the parties to make such a contract, and the question is merely as to what they mean; that is, what is to be imputed to the words they used. Whatever plausibility there is in the argument, is in the fact that the defendant must have known the predicament in which the contractors would be put if it withdrew its offer after the bids went in. However, it seems entirely clear that the contractors did not suppose that they accepted the offer merely by putting in their bids. If, for example, the successful one had repudiated the contract with the public authorities after it had been awarded to him, certainly the defendant could not have sued him for a breach. If he had become bankrupt, the defendant could not prove against his estate. It seems plain therefore that there was no contract between them. And if there be any doubt as to this, the language of the offer sets it at rest. The phrase, "if successful in being awarded this contract," is scarcely met by the mere use of the prices in the bids. Surely such a use was not an "award" of the contract to the defendant. Again, the phrase, "we are offering these prices for . . . prompt acceptance after the general contract has been awarded," looks to the usual communication of an acceptance, and precludes the idea that the use of the offer in the bidding shall be the equivalent. It may indeed be argued that this last

language contemplated no more than an early notice that the offer had been accepted, the actual acceptance being the bid, but that would wrench its natural meaning too far, especially in the light of the preceding phrase. The contractors had a ready escape from their difficulty by insisting upon a contract before they used the figures; and in commercial transactions it does not in the end promote justice to seek strained interpretations in aid of those who do not protect themselves.

But the plaintiff says that even though no bilateral contract was made, the defendant should be held under the doctrine of "promissory estoppel." This is to be chiefly found in those cases where persons subscribe to a venture, usually charitable, and are held to their promises after it has been completed. It has been applied much more broadly, however, and has now been generalized in section 90, of the Restatement of Contracts. We may arguendo accept it as it there reads, for it does not apply to the case at bar. Offers are ordinarily made in exchange for a consideration, either a counter-promise or some other act which the promisor wishes to secure. In such cases they propose bargains; they presuppose that each promise or performance is an inducement to the other. *Wisconsin, etc., Ry. v. Powers*, 191 U.S. 379, 386, 387, 24 S. Ct. 107, 48 L. Ed. 229; *Banning Co. v. California*, 240 U.S. 142, 152, 153, 36 S. Ct. 338, 60 L. Ed. 569. But a man may make a promise without expecting an equivalent; a donative promise, conditional or absolute. The common law provided for such by sealed instruments, and it is unfortunate that these are no longer generally available. The doctrine of "promissory estoppel" is to avoid the harsh results of allowing the promisor in such a case to repudiate, when the promisee has acted in reliance upon the promise. *Siegel v. Spear & Co.*, 234 N.Y. 479, 138 N.E. 414, 26 A.L.R. 1205. Cf. *Allegheny College v. National Bank*, 246 N.Y. 369, 159 N.E. 173, 57 L.R.A. 980. But an offer for an exchange is not meant to become a promise until a consideration has been received, either a counter-promise or whatever else is stipulated. To extend it would be to hold the offeror regardless of the stipulated condition of his offer. In the case at bar the defendant offered to deliver the linoleum in exchange for the plaintiff's acceptance, not for its bid, which was a matter of indifference to it. That offer could become a promise to deliver only when the equivalent was received; that is, when the plaintiff promised to take and pay for it. There is no room in such a situation for the doctrine of "promissory estoppel."

Nor can the offer be regarded as of an option, giving the plaintiff the right seasonably to accept the linoleum at the quoted prices if its bid was accepted, but not binding it to take and pay, if it could get a better bargain elsewhere. There is not the least reason to suppose that the defendant meant to subject itself to such a one-sided obligation. True, if so construed, the doctrine of "promissory estoppel" might apply, the plaintiff having acted in reliance upon it, though, so far as we have found, the decisions are otherwise. *Ganss v. Guffey Petroleum Co.*, 125 A.D. 760,

110 N.Y.S. 176; *Comstock v. North*, 88 Miss. 754, 41 So. 374. As to that, however, we need not declare ourselves.

Judgment affirmed.

NOTE

Should the mistaken bid case be handled by manipulating the consideration doctrine? The case is noted in 28 Ill. L. Rev. 419 (1933); 20 Va. L. Rev. 214 (1933).

An interesting case study of the problems in the building industry is Schultz, *The Firm Offer Puzzle: A Study of Practices in the Construction Industry*, 19 U. Chi. L. Rev. 237 (1952), discussing the Indiana construction industry; for a more recent discussion of the Virginia construction industry, see Note, *Another Look at Construction Building Contracts and Formation*, 53 Va. L. Rev. 1270 (1967). See further, *Recent Cases*, 62 Harv. L. Rev. 693 (1949); Sharp, *Promises, Mistake and Reciprocity*, 19 U. Chi. L. Rev. 286 (1952); Keys, *Consideration Reconsidered — The Problems of the Withdrawn Bid*, 10 Stan. L. Rev. 441 (1958); Note, 39 N.Y.U. L. Rev. 816 (1964); 37 U. Chi. L. Rev. 798 (1968); J. Dawson, W. Harvey & S. Henderson, *Cases and Comment on Contracts* 352 (4th ed. 1982).

Williams v. Favret, 161 F. 822 (5th Cir. 1947), discussed in the Schultz article, involved a suit by a subcontractor (sub) against a general contractor (general). The quotation of the sub solicited by the general contained the following clause: "If our estimate used, wire us collect prior to June 6 or else same is withdrawn." General sent the following wire back: "June 6 we used your bid." After being awarded the contract, general gave the contract to another sub. Is the quotation an offer? Is the wire of June 6 an acceptance? See 1 Corbin §24, n.11 (1963).

For a discussion of the revocability of offers submitted to municipal corporations under statutory competitive bidding, see 47 Mich. L. Rev. 1220 (1949), discussing *Conduit & Foundation Corporation v. Atlantic City*, 2 N.J. Super. 433, 64 A.2d 382 (1949). See further, 1 Corbin §46 (1963). For the firm-bid rule in contracts with the federal government, see, e.g., *Refining Associates, Inc. v. United States*, 109 F.Supp. 259 (1953), noted in 66 Harv. L. Rev. 1312 (1953).

DRENNAN v. STAR PAVING CO.

51 Cal. 2d 409, 333 P.2d 757 (1958)

TRAYNOR, J. — Defendant appeals from a judgment for plaintiff in an action to recover damages caused by defendant's refusal to perform certain paving work according to a bid it submitted to plaintiff.

On July 28, 1955, plaintiff, a licensed general contractor, was preparing a bid on the "Monte Vista School Job" in the Lancaster school district. Bids had to be submitted before 8 p. m. Plaintiff testified that it was customary in that area for general contractors to receive the bids of subcontractors by telephone on the day set for bidding and to rely on them in computing their own bids. Thus on that day plaintiff's secretary, Mrs. Johnson, received by telephone between 50 and 75 subcontractors' bids for various parts of the school job. As each bid came in, she wrote it on a special form, which she brought into plaintiff's office. He then posted it on a master cost sheet setting forth the names and bids of all subcontractors. His own bid had to include the names of subcontractors who were to perform one-half of one per cent or more of the construction work, and he had also to provide a bidder's bond of 10 per cent of his total bid of \$317,385 as a guarantee that he would enter the contract if awarded the work.

Later in the afternoon, Mrs. Johnson had a telephone conversation with Kenneth R. Hoon, an estimator for defendant. He gave his name and telephone number and stated that he was bidding for defendant for the paving work at the Monte Vista School according to plans and specifications and that his bid was \$7,131.60. At Mrs. Johnson's request he repeated his bid. Plaintiff listened to the bid over an extension telephone in his office and posted it on the master sheet after receiving the bid form from Mrs. Johnson. Defendant's was the lowest bid for the paving. Plaintiff computed his own bid accordingly and submitted it with the name of defendant as the subcontractor for the paving. When the bids were opened on July 28th, plaintiff's proved to be the lowest, and he was awarded the contract.

On his way to Los Angeles the next morning plaintiff stopped at defendant's office. The first person he met was defendant's construction engineer, Mr. Oppenheimer. Plaintiff testified:

I introduced myself and he immediately told me that they had made a mistake in their bid to me the night before, they couldn't do it for the price they had bid, and I told him I would expect him to carry through with their original bid because I had used it in compiling my bid and the job was being awarded them. And I would have to go and do the job according to my bid and I would expect them to do the same.

Defendant refused to do the paving work for less than \$15,000. Plaintiff testified that he "got figures from other people" and after trying for several months to get as low a bid as possible engaged L & H Paving Company, a firm in Lancaster, to do the work for \$10,948.60.

The trial court found on substantial evidence that defendant made a definite offer to do the paving on the Monte Vista job according to the plans and specifications for \$7,131.60, and that plaintiff relied on defen-

dant's bid in computing his own bid for the school job and naming defendant therein as the subcontractor for the paving work. Accordingly, it entered judgment for plaintiff in the amount of \$3,817 (the difference between defendant's bid and the cost of the paving to plaintiff) plus costs.

Defendant contends that there was no enforceable contract between the parties on the ground that it made a revocable offer and revoked it before plaintiff communicated his acceptance to defendant.

There is no evidence that defendant offered to make its bid irrevocable in exchange for plaintiff's use of its figures in computing his bid. Nor is there evidence that would warrant interpreting plaintiff's use of defendant's bid as the acceptance thereof, binding plaintiff, on condition he received the main contract, to award the subcontract to defendant. In sum, there was neither an option supported by consideration nor a bilateral contract binding on both parties.

Plaintiff contends, however, that he relied to his detriment on defendant's offer and that defendant must therefore answer in damages for its refusal to perform. Thus the question is squarely presented: Did plaintiff's reliance make defendant's offer irrevocable?

Section 90 of the Restatement of Contracts states: "A promise which the promisor should reasonably expect to induce action or forbearance of a definite and substantial character on the part of the promisee and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise." This rule applies in this state. [Citations.]

Defendant's offer constituted a promise to perform on such conditions as were stated expressly or by implication therein or annexed thereto by operation of law. (See 1 Williston, Contracts [3d ed.], §24A, p. 56, §61, p. 196.) Defendant had reason to expect that if its bid proved the lowest it would be used by plaintiff. It induced "action . . . of a definite and substantial character on the part of the promisee."

Had defendant's bid expressly stated or clearly implied that it was revocable at any time before acceptance we would treat it accordingly. It was silent on revocation, however, and we must therefore determine whether there are conditions to the right of revocation imposed by law or reasonably inferable in fact. In the analogous problem of an offer for a unilateral contract, the theory is now obsolete that the offer is revocable at any time before complete performance. Thus section 45 of the Restatement of Contracts provides:

If an offer for a unilateral contract is made, and part of the consideration requested in the offer is given or tendered by the offeree in response thereto, the offeror is bound by contract, the duty of immediate performance of which is conditional on the full consideration being given or tendered within the time stated in the offer, or, if no time is stated therein, within a reasonable time.

In explanation, comment *b* states that the

main offer includes as a subsidiary promise, necessarily implied, that if part of the requested performance is given, the offeror will not revoke his offer, and that if tender is made it will be accepted. Part performance or tender may thus furnish consideration for the subsidiary promise. Moreover, merely acting in justifiable reliance on an offer may in some cases serve as sufficient reason for making a promise binding (see §90).

Whether implied in fact or law, the subsidiary promise serves to preclude the injustice that would result if the offer could be revoked after the offeree had acted in detrimental reliance thereon. Reasonable reliance resulting in a foreseeable prejudicial change in position affords a compelling basis also for implying a subsidiary promise not to revoke an offer for a bilateral contract.

The absence of consideration is not fatal to the enforcement of such a promise. It is true that in the case of unilateral contracts the Restatement finds consideration for the implied subsidiary promise in the part performance of the bargained-for exchange, but its reference to section 90 makes clear that consideration for such a promise is not always necessary. The very purpose of section 90 is to make a promise binding even though there was no consideration "in the sense of something that is bargained for and given in exchange." (See 1 Corbin, Contracts 634 et seq.) Reasonable reliance serves to hold the offeror in lieu of the consideration ordinarily required to make the offer binding. In a case involving similar facts the Supreme Court of South Dakota stated that

we believe that reason and justice demand that the doctrine [of section 90] be applied to the present facts. We cannot believe that by accepting this doctrine as controlling in the state of facts before us we will abolish the requirement of a consideration in contract cases, in any different sense than an ordinary estoppel abolishes some legal requirement in its application. We are of the opinion, therefore, that the defendants in executing the agreement [which was not supported by consideration] made a promise which they should have reasonably expected would induce the plaintiff to submit a bid based thereon to the Government, that such promise did induce this action, and that injustice can be avoided only by enforcement of the promise.

(Northwestern Engineering Co. v. Ellerman, 69 S.D. 397, 408 [10 N.W.2d 879]; see also Robert Gordon, Inc. v. Ingersoll-Rand Co., 117 F.2d 654, 661; cf. James Baird Co. v. Gimbel Bros., 64 F.2d 344.)

When plaintiff used defendant's offer in computing his own bid, he bound himself to perform in reliance on defendant's terms. Though defendant did not bargain for this use of its bid neither did defendant make it idly, indifferent to whether it would be used or not. On the contrary it is

reasonable to suppose that defendant submitted its bid to obtain the subcontract. It was bound to realize the substantial possibility that its bid would be the lowest, and that it would be included by plaintiff in his bid. It was to its own interest that the contractor be awarded the general contract; the lower the subcontract bid, the lower the general contractor's bid was likely to be and the greater its chance of acceptance and hence the greater defendant's chance of getting the paving subcontract. Defendant had reason not only to expect plaintiff to rely on its bid but to want him to. Clearly defendant had a stake in plaintiff's reliance on its bid. Given this interest and the fact that plaintiff is bound by his own bid, it is only fair that plaintiff should have at least an opportunity to accept defendant's bid after the general contract has been awarded to him.

It bears noting that a general contractor is not free to delay acceptance after he has been awarded the general contract in the hope of getting a better price. Nor can he reopen bargaining with the subcontractor and at the same time claim a continuing right to accept the original offer. (See *R. J. Daum Const. Co. v. Child*, 122 Utah 194 [247 P.2d 817, 823].) In the present case plaintiff promptly informed defendant that plaintiff was being awarded the job and that subcontract was awarded to defendant.

Defendant contends, however, that its bid was the result of mistake and that it was therefore entitled to revoke it. It relies on the rescission cases of *M. F. Kemper Const. Co. v. City of Los Angeles*, 37 Cal. 2d 696 [235 P.2d 7], and *Brunzell Const. Co. v. G. J. Weisbrod, Inc.*, 134 Cal. App. 2d 278 [285 P.2d 989]. (See also *Lemoge Electric v. San Mateo County*, 46 Cal. 2d 659, 662 [297 P.2d 638].) In those cases, however, the bidder's mistake was known or should have been to the offeree, and the offeree could be placed in status quo. Of course, if plaintiff had reason to believe that defendant's bid was in error, he could not justifiably rely on it, and section 90 would afford no basis for enforcing it. (*Robert Gordon, Inc. v. Ingersoll-Rand Co.*, 117 F.2d 654, 660.) Plaintiff, however, had no reason to know that defendant had made a mistake in submitting its bid, since there was usually a variance of 160 per cent between the highest and lowest bids for paving in the desert around Lancaster. He committed himself to performing the main contract in reliance on defendant's figures. Under these circumstances defendant's mistake, far from relieving it of its obligation, constitutes an additional reason for enforcing it, for it misled plaintiff as to the cost of doing the paving. Even had it been clearly understood that defendant's offer was revocable until accepted, it would not necessarily follow that defendant had no duty to exercise reasonable care in preparing its bid. It presented its bid with knowledge of the substantial possibility that it would be used by plaintiff; it could foresee the harm that would ensue from an erroneous underestimate of the cost. Moreover, it was motivated by its own business interest. Whether or not these considerations alone would justify recovery for negligence had the case been tried on that theory (see *Biakanja v. Irving*, 49 Cal. 2d 647, 650

[320 P.2d 16]), they are persuasive that defendant's mistake should not defeat recovery under the rule of section 90 of the Restatement of Contracts.

As between the subcontractor who made the bid and the general contractor who reasonably relied on it, the loss resulting from the mistake should fall on the party who caused it.

Leo F. Piazza Paving Co. v. Bebek & Brkich, 141 Cal. App. 2d 226 [296 P.2d 368], and *Bard v. Kent*, 19 Cal. 2d 499 [122 P.2d 8, 139], are not to the contrary. In the *Piazza* case the court sustained a finding that defendants intended, not to make a firm bid, but only to give the plaintiff "some kind of an idea to use" in making its bid; there was evidence that the defendants had told plaintiff they were unsure of the significance of the specifications. There was thus no offer, promise, or representation on which the defendants should reasonably have expected the plaintiff to rely. The *Bard* case held that an option not supported by consideration was revoked by the death of the optioner. The issue of recovery under the rule of section 90 was not pleaded at the trial, and it does not appear that the offeree's reliance was "of a definite and substantial character" so that injustice could be avoided "only by the enforcement of the promise."

There is no merit in defendant's contention that plaintiff failed to state a cause of action, on the ground that the complaint failed to allege that plaintiff attempted to mitigate the damages or that they could not have been mitigated. Plaintiff alleged that after defendant's default, "plaintiff had to procure the services of the L & H Co. to perform said asphaltic paving for the sum of \$10,948.60." Plaintiff's uncontradicted evidence showed that he spent several months trying to get bids from other subcontractors and that he took the lowest bid. Clearly he acted reasonably to mitigate damages. In any event any uncertainty in plaintiff's allegation as to damages could have been raised by special demurrer. (Code Civ. Proc., §430, subd. 9.) It was not so raised and was therefore waived. (Code Civ. Proc., §434.)

The judgment is affirmed.

**EASTERN AIR LINES, INC. v.
GULF OIL CORP.**

415 F. Supp. 429 (S.D. Fla. 1975)

JAMES LAWRENCE KING, District Judge.
Eastern Air Lines, Inc., hereafter Eastern, and Gulf Oil Corporation,

hereafter Gulf, have enjoyed a mutually advantageous business relationship involving the sale and purchase of aviation fuel for several decades.

This controversy involves the threatened disruption of that historic relationship and the attempt, by Eastern, to enforce the most recent contract between the parties. On March 8, 1974 the correspondence and telex communications between the corporate entities culminated in a demand by Gulf that Eastern must meet its demand for a price increase or Gulf would shut off Eastern's supply of jet fuel within fifteen days.

Eastern responded by filing its complaint with this court, alleging that Gulf had breached its contract and requesting preliminary and permanent mandatory injunctions requiring Gulf to perform the contract in accordance with its terms. By agreement of the parties, a preliminary injunction preserving the status quo was entered on March 20, 1974, requiring Gulf to perform its contract and directing Eastern to pay in accordance with the contract terms, pending final disposition of the case.

Gulf answered Eastern's complaint, alleging that the contract was not a binding requirements contract, was void for want of mutuality, and, furthermore, was "commercially impracticable" within the meaning of Uniform Commercial Code §2-615; Fla. Stat. §§672.614 and 672.615.

The extraordinarily able advocacy by the experienced lawyers for both parties produced testimony at the trial from internationally respected experts who described in depth economic events that have, in recent months, profoundly affected the lives of every American.

THE CONTRACT

On June 27, 1972, an agreement was signed by the parties which, as amended, was to provide the basis upon which Gulf was to furnish jet fuel to Eastern at certain specific cities in the Eastern system. Said agreement supplemented an existing contract between Gulf and Eastern which, on June 27, 1972, had approximately one year remaining prior to its expiration.

The contract is Gulf's standard form aviation fuel contract and is identical in all material particulars with the first contract for jet fuel, dated 1959, between Eastern and Gulf and, indeed, with aviation fuel contracts antedating the jet age. It is similar to contracts in general use in the aviation fuel trade. The contract was drafted by Gulf after substantial arm's length negotiation between the parties. Gulf approached Eastern more than a year before the expiration of the then-existing contracts between Gulf and Eastern, seeking to preserve its historic relationship with Eastern. Following several months of negotiation, the contract, consolidating and extending the terms of several existing contracts, was executed by the parties in June, 1972, to expire January 31, 1977.

The parties agreed that this contract, as its predecessor, should provide a reference to reflect changes in the price of the raw material from which jet fuel is processed, i.e., crude oil, in direct proportion to the cost per gallon of jet fuel.

Both parties regarded the instant agreement as favorable, Eastern, in part, because it offered immediate savings in projected escalations under the existing agreement through reduced base prices at the contract cities; while Gulf found a long term outlet for a capacity of jet fuel coming on stream from a newly completed refinery, as well as a means to relate anticipated increased cost of raw material (crude oil) directly to the price of the refined product sold. The previous Eastern/Gulf contracts contained a price index clause which operated to pass on to Eastern only one-half of any increase in the price of crude oil. Both parties knew at the time of contract negotiations that increases in crude oil prices would be expected, were "a way of life," and intended that those increases be borne by Eastern in a direct proportional relationship of crude oil cost per barrel to jet fuel cost per gallon.

Accordingly, the parties selected an indicator (West Texas Sour); a crude which is bought and sold in large volume and was thus a reliable indicator of the market value of crude oil. From June 27, 1972 to the fall of 1973, there were in effect various forms of U.S. government imposed price controls which at once controlled the price of crude oil generally, West Texas Sour specifically, and hence the price of jet fuel. As the government authorized increased prices of crude those increases were in turn reflected in the cost of jet fuel. Eastern has paid a per gallon increase under the contract from 11 cents to 15 cents (or some 40%).

The indicator selected by the parties was "the average of the posted prices for West Texas sour crude, 30.0-30.9 gravity of Gulf Oil Corporation, Shell Oil Company, and Pan American Petroleum Corporation." The posting of crude prices under the contract "shall be as listed for these companies in Platts Oilgram Service — Crude Oil Supplement . . ."

"Posting" has long been a practice in the oil industry. It involves the physical placement at a public location of a price bulletin reflecting the current price at which an oil company will pay for a given barrel of a specific type of crude oil. Those posted price bulletins historically have, in addition to being displayed publicly, been mailed to those persons evincing interest therein, including sellers of crude oil, customers whose price of product may be based thereon, and, among others, Platts Oilgram, publishers of a periodical of interest to those related to the oil industry.

In recent years, the United States has become increasingly dependent upon foreign crude oil, particularly from the "OPEC" nations most of which are in the Middle East. OPEC was formed in 1970 for the avowed purpose of raising oil prices, and has become an increasingly cohesive and potent organization as its member nations have steadily enhanced

their equity positions and their control over their oil production facilities. Nationalization of crude oil resources and shutdowns of production and distribution have become a way of life for oil companies operating in OPEC nations, particularly in the volatile Middle East. The closing of the Suez Canal and the concomitant interruption of the flow of Mid-East oil during the 1967 "Six-Day War," and Libya's nationalization of its oil industry during the same period, are only some of the more dramatic examples of a trend that began years ago. By 1969 "the handwriting was on the wall" in the words of Gulf's foreign oil expert witness, Mr. Blackledge.

During 1970 domestic United States oil production "peaked;" since then it has declined while the percentage of imported crude oil has been steadily increasing. Unlike domestic crude oil, which has been subject to price control since August 15, 1971, foreign crude oil has never been subject to price control by the United States Government. Foreign crude oil prices, uncontrolled by the Federal Government, were generally lower than domestic crude oil prices in 1971 and 1972; during 1973 foreign prices "crossed" domestic prices; by late 1973 foreign prices were generally several dollars per barrel higher than controlled domestic prices. It was during late 1973 that the Mid-East exploded in another war, accompanied by an embargo (at least officially) by the Arab oil-producing nations against the United States and certain of its allies. World prices for oil and oil products increased.

Mindful of that situation and for various other reasons concerning the nation's economy, the United States government began a series of controls affecting the oil industry culminating, in the fall of 1973, with the implementation of price controls known as "two-tier." In practice "two-tier" can be described as follows: taking as the bench mark the number of barrels produced from a given well in May of 1972, that number of barrels is deemed "old" oil. The price of "old" oil then is frozen by the government at a fixed level. To the extent that the productivity of a given well can be increased over the May, 1972, production, that increased production is deemed "new" oil. For each barrel of "new" oil produced, the government authorized the release from price controls of an equivalent number of barrels from those theretofore designated "old" oil. For example, from a well which in May of 1972, produced 100 barrels of oil; all of the production of that well would, since the imposition of "two-tier" in August of 1973, be "old" oil. Increased productivity to 150 barrels would result in 50 barrels of "new" oil and 50 barrels of "released" oil; with the result that 100 barrels of the 150 barrels produced from the well would be uncontrolled by the "two-tier" pricing system, while the 50 remaining barrels of "old" would remain government price controlled.

The implementation of "two-tier" was completely without precedent in the history of government price control action. Its impact, however, was nominal, until the imposition of an embargo upon the exportation of

crude oil by certain Arab countries in October, 1973. Those countries deemed sympathetic to Israel were embargoed from receiving oil from the Arab oil producing countries. The United States was among the principal countries affected by that embargo, with the result that it experienced an immediate "energy crisis."

Following closely after the embargo, OPEC (Oil Producing Export Countries) unilaterally increased the price of their crude to the world market some 400% between September, 1973, and January 15, 1974. Since the United States domestic production was at capacity, it was dependent upon foreign crude to meet its requirements. New and released oil (uncontrolled) soon reached parity with the price of foreign crude, moving from approximately \$5 to \$11 a barrel from September, 1974 to January 15, 1975.

Since imposition of "two-tier," the price of "old oil" has remained fixed by government action, with the oil companies resorting to postings reflecting prices they will pay for the new and released oil, not subject to government controls. Those prices, known as "premiums," are the subject of supplemental bulletins which are likewise posted by the oil companies and furnished to interested parties, including Platts Oilgram.

Platts, since the institution of "two-tier" has not published the posted prices of any of the premiums offered by the oil companies in the United States, including those of Gulf Oil Corporation, Shell Oil Company and Pan American Petroleum, the companies designated in the agreement. The information which has appeared in Platts since the implementation of "two-tier" with respect to the price of West Texas Sour crude oil has been the price of "old" oil subject to government control.

Under the court's restraining order, entered in this cause by agreement of the parties, Eastern has been paying for jet fuel from Gulf on the basis of the price of "old" West Texas Sour crude oil as fixed by government price control action, i.e., \$5 a barrel. Approximately 40 gallons of finished jet fuel product can be refined from a barrel of crude.

Against this factual background we turn to a consideration of the legal issues.

I. THE "REQUIREMENTS" CONTRACT

Gulf has taken the position in this case that the contract between it and Eastern is not a valid document in that it lacks mutuality of obligation; it is vague and indefinite; and that it renders Gulf subject to Eastern's whims respecting the volume of jet fuel Gulf would be required to deliver to the purchaser Eastern.

The contract talks in terms of fuel "requirements." The parties have interpreted this provision to mean that any aviation fuel purchased by Eastern at one of the cities covered by the contract, must be bought from

Gulf. Conversely, Gulf must make the necessary arrangements to supply Eastern's reasonable good faith demands at those same locations. This is the construction the parties themselves have placed on the contract and it has governed their conduct over many years and several contracts.

In early cases, requirements contracts were found invalid for want of the requisite definiteness, or on the grounds of lack of mutuality. Many such cases are collected and annotated at 14 A.L.R. 1300.

As reflected in the foregoing annotation, there developed rather quickly in the law the view that a requirements contract could be binding where the purchaser had an operating business. The "lack of mutuality" and "indefiniteness" were resolved since the court could determine the volume of goods provided for under the contract by reference to objective evidence of the volume of goods required to operate the specified business. Therefore, well prior to the adoption of the Uniform Commercial Code, case law generally held requirements contracts binding. See 26 A.L.R.2d 1099, 1139.

The Uniform Commercial Code, adopted in Florida in 1965, specifically approves requirements contracts in F.S. 672.306 (U.C.C. §2-306(1)).

(1) A term which measures the quantity by the output of the seller or the requirements of the buyer means such actual output or requirements as may occur in good faith, except that no quantity unreasonably disproportionate to any stated estimate or in the absence of a stated estimate to any normal or otherwise comparable prior output or requirements may be tendered or demanded.

The Uniform Commercial Code Official Comment interprets §2-306(1) as follows:

2. Under this Article, a contract for output or requirements is not too indefinite since it is held to mean the actual good faith output or requirements of the particular party. Nor does such a contract lack mutuality of obligation since, under this section, the party who will determine quantity is required to operate his plant or conduct his business in good faith and according to commercial standards of fair dealing in the trade so that his output or requirements will approximate a reasonably foreseeable figure. Reasonable elasticity in the requirements is expressly envisaged by this section and good faith variations from prior requirements are permitted even when the variation may be such as to result in discontinuance. A shut-down by a requirements buyer for lack of orders might be permissible when a shut-down merely to curtail losses would not. The essential test is whether the party is acting in good faith. Similarly, a sudden expansion of the plant by which requirements are to be measured would not be included within the scope of the contract as made but normal expansion undertaken in good faith would be within the scope of this section. One of the factors in an expansion situation would be whether the market price has risen greatly in a case in which the requirements contract contained a fixed price. Rea-

sonable variation of an extreme sort is exemplified in *Southwest Natural Gas Co. v. Oklahoma Portland Cement Co.*, 102 F.2d 630 (C.C.A. 10, 1939).

Some of the prior Gulf-Eastern contracts have included the estimated fuel requirements for some cities covered by the contract while others have none. The particular contract contains an estimate for Gainesville, Florida requirement.

The parties have consistently over the years relied upon each other to act in good faith in the purchase and sale of the required quantities of aviation fuel specified in the contract. During the course of the contract, various estimates have been exchanged from time to time, and, since the advent of the petroleum allocations programs, discussions of estimated requirements have been on a monthly (or more frequent) basis.

The court concludes that the document is a binding and enforceable requirements contract.

II. BREACH OF CONTRACT

Gulf suggests that Eastern violated the contract between the parties by manipulating its requirements through a practice known as "fuel freighting" in the airline industry. Requirements can vary from city to city depending on whether or not it is economically profitable to freight fuel. This fuel freighting practice in accordance with price could affect lifting from Gulf stations by either raising such liftings or lowering them. If the price was higher at a Gulf station, the practice could have reduced liftings there by lifting fuel in excess of its actual operating requirements at a prior station, and thereby not loading fuel at the succeeding high price Gulf station. Similarly where the Gulf station was comparatively cheaper, an aircraft might load more heavily at the Gulf station and not load at other succeeding non-Gulf stations.

The court however, finds that Eastern's performance under the contract does not constitute a breach of its agreement with Gulf and is consistent with good faith and established commercial practices as required by U.C.C. §2-306.

"Good Faith" means "honesty in fact in the conduct or transaction concerned" U.C.C. §1-201(19). Between merchants, "good faith" means "honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade"; U.C.C. §2-103(1)(b) and Official Comment 2 of U.C.C. §2-306. The relevant commercial practices are "courses of performance," "courses of dealing" and "usages of trade."

Throughout the history of commercial aviation, including 30 years of dealing between Gulf and Eastern, airlines' liftings of fuel by nature have been subject to substantial daily, weekly, monthly and seasonal varia-

tions, as they are affected by weather, schedule changes, size of aircraft, aircraft load, local airport conditions, ground time, availability of fueling facilities, whether the flight is on time or late, passenger convenience, economy and efficiency of operation, fuel taxes, into-plane fuel service charges, fuel price, and, ultimately, the judgment of the flight captain as to how much fuel he wants to take.

All these factors are, and for years have been, known to oil companies, including Gulf, and taken into account by them in their fuel contracts. Gulf's witnesses at trial pointed to certain examples of numerically large "swings" in monthly liftings by Eastern at various Gulf stations. Gulf never complained of this practice and apparently accepted it as normal procedure. Some of the "swings" were explained by the fueling of a single aircraft for one flight, or by the addition of one schedule in mid-month. The evidence establishes that Eastern, on one occasion, requested 500,000 additional gallons for one month at one station, without protest from Gulf, and that Eastern increased its requirements at another station more than 50 percent year to year, from less than 2,000,000 to more than 3,000,000 gallons, again, without Gulf objection.

The court concludes that fuel freighting is an established industry practice, inherent in the nature of the business. The evidence clearly demonstrated that the practice has long been part of the established courses of performance and dealing between Eastern and Gulf. As the practice of "freighting" or "tankering" has gone on unchanged and unchallenged for many years accepted as a fact of life by Gulf without complaint, the court is reminded of Official Comment 1 to U.C.C. §2-208:

The parties themselves know best what they have meant by their words of agreement and their action under that agreement is the best indication of what that meaning was.

From a practical point of view, "freighting" opportunities are very few, according to the uncontradicted testimony, as the airline must perform its schedules in consideration of operating realities. There is no suggestion here that Eastern is operating at certain Gulf stations but taking no fuel at all. The very reason Eastern initially desired a fuel contract was because the airline planned to take on fuel, and had to have an assured source of supply.

If a customer's demands under a requirements contract become excessive, U.C.C. §2-306 protects the seller and, in the appropriate case, would allow him to refuse to deliver unreasonable amounts demanded (but without eliminating his basic contract obligation); similarly, in an appropriate case, if a customer repeatedly had no requirements at all, the seller might be excused from performance if the buyer suddenly and without warning should descend upon him and demand his entire inventory, but the court is not called upon to decide those cases here.

Rather, the case here is one where the established courses of performance and dealing between the parties, the established usages of the trade, and the basic contract itself all show that the matter complained of for the first time by Gulf after commencement of this litigation are the fundamental given ingredients of the aviation fuel trade to which the parties have accommodated themselves successfully and without dispute over the years.

The practical interpretation given to their contracts by the parties to them while they are engaged in their performance, and before any controversy has arisen concerning them, is one of the best indications of their true intent, and courts that adopt and enforce such a construction are not likely to commit serious error.

Manhattan Life Ins. Co. of New York v. Wright, 126 F. 82, 87 (8th Cir. 1903). Accord, *Spindler v. Kushner*, 284 So. 2d 481, 484 (Fla. App. 1973).

The court concludes that Eastern has not violated the contract.

III. COMMERCIAL IMPRACTICABILITY

[The court found that Gulf had not discharged its burden of proof in attempting to establish that the contract was commercially impracticable, and held that both the rise in foreign oil prices and the "two-tier" system of price control were foreseeable at the time the contract was made. On commercial impracticability, see Chapter 8 *infra*. The court's opinion on this matter is fascinating and gives a glimpse into the workings of a major oil company. It is recommended reading.]

IV. REMEDY

Having found and concluded that the contract is a valid one, should be enforced, and that no defenses have been established against it, there remains for consideration the proper remedy.

The Uniform Commercial Code provides that in an appropriate case specific performance may be decreed. This case is a particularly appropriate one for specific performance. The parties have been operating for more than a year pursuant to a preliminary injunction requiring specific performance of the contract and Gulf has stipulated that it is able to perform. Gulf presently supplies Eastern with 100,000,000 gallons of fuel annually or 10 percent of Eastern's total requirements. If Gulf ceases to supply this fuel, the result will be chaos and irreparable damage.

Under the U.C.C. a more liberal test in determining entitlement to specific performance has been established than the test one must meet

for classic equitable relief. U.C.C. §2-716(1); *Kaiser Trading Co. v. Associated Metals & Minerals Corp.*, 321 F. Supp. 923, 932 (N.D. Cal. 1970), *appeal dismissed per curiam*, 443 F.2d 1364 (9th Cir. 1971).

It has previously been found and concluded that Eastern is entitled to Gulf's fuel at the prices agreed upon in the contract. In the circumstances, a decree of specific performance becomes the ordinary and natural relief rather than the extraordinary one. The parties are before the court, the issues are squarely framed, they have been clearly resolved in Eastern's favor, and it would be a vain, useless and potentially harmful exercise to declare that Eastern has a valid contract, but leave the parties to their own devices. Accordingly, the preliminary injunction heretofore entered is made a permanent injunction and the order of this court herein.

UTAH INTERNATIONAL INC. v. COLORADO-UTE ELECTRIC ASSN., INC.

425 F. Supp. 1093 (D. Colo. 1976)

MEMORANDUM OPINION AND ORDER

ARRAJ, District Judge.

Plaintiff Utah International, a mining company with international operations, brings this declaratory judgment action against Colorado-Ute Electric Association, Inc., Platte River Power Authority, Tri-State Generation and Transmission Association, and Salt River Project Agriculture Improvement and Power District, all wholesalers of electric power and energy. Plaintiff seeks a declaration of its rights and duties as a party to a contract for the sale of coal, and defendants have counter-claimed for the specific performance of that contract.

The contract in question is a thirty five year requirements contract containing a maximum sales obligation and minimum purchase obligation. Plaintiff as seller claims that defendants have breached the contract by building electric generating units with generating capacities larger than specified in the sales contract. As a result of such construction, plaintiff contends that it will be required to provide more coal than was anticipated by this requirements contract and that its contractual obligations thereunder should, therefore, be terminated. Trial was to the Court and this Opinion shall constitute the findings of facts and conclusions of law in conformance with Fed. R. Civ. P. 52(a).

In 1969, the four defendants, along with Public Service Company of Colorado, Intermountain Consumers Power Association, and Arizona Public Service formed the Western Colorado Resource Study to consider the possibility of constructing coal-fired electric generating units near Craig, Colorado. This project later became known as the Yampa Project.

These original participants appointed a Steering Committee to be in overall charge of the project, the membership consisting of senior executives of each defendant and representatives of the United States Bureau of Reclamation. This committee in turn created a task force system to carry out specific study assignments.

On April 13, 1970 the participants commenced negotiations with plaintiff for the supply of fuel for the Yampa Project and sent to plaintiff, and to other prospective suppliers an invitation to submit proposals for the mining and delivery of coal fuel. The amount of coal contemplated as necessary to fuel the project was at that time undetermined but the participants provided coal consumption estimates for the different unit alternatives then being considered. In response, plaintiff proposed a pricing schedule based on calculations made from the estimated coal consumption figures provided by defendants in their invitation.

In December of 1970, defendant Salt River, as the participant in charge of the initial purchase negotiations for the project's turbine-generators, obtained a quotation from General Electric for two 450,000 kilowatt generators. In March of the following year, Salt River and General Electric executed a letter of intent for these generators with the stipulation that the size of the units could subsequently be changed.

By early 1971 Public Service Company of Colorado, Intermountain Consumers Power Association, and Arizona Public Service Company had withdrawn from the Western Colorado Resource Study leaving the defendants as the remaining participants. As a result of that withdrawal the participants began re-evaluating their projected consumer power demands and their plans regarding the size of the generating units to be constructed. By December of 1971 they had decided that two units, each rated at 350,000 kilowatts net, would be capable of providing the generating capacity necessary to meet their re-evaluated projections.

In choosing the machine to meet their needs, defendants operated under certain assumptions generally accepted by the electrical generating industry. The first and most important assumption is that a generating unit of the type being installed at Craig will not operate at 100% capacity but rather at approximately 75% capacity over an extended period, such as the thirty five year term of this contract. The reason for this is that all such machines require regularly scheduled maintenance periods and also periods of unanticipated maintenance during which it is necessary to shut down the machines.

Once the unit size was chosen, the parties then calculated the amount of coal that such units would burn over thirty five years. This process was a joint effort between representatives of the defendants and representatives of the plaintiff. Both parties used the net figure 350,000 kilowatts as a starting point in estimating the probable coal consumption and then communicated their calculations to the other party for verification. Grad-

ually, through this process, the estimates became refined, and both parties as of May of 1972 understood that there would be constructed two generators of approximately 350,000 kilowatt net capacity each, which machines would operate at an average capacity factor of about 75% and would burn approximately 76 million tons of coal over the life of the contract. It was additionally understood that the generating units would operate at almost 90% capacity during the first ten years of the contract and then steadily decline in capacity during the balance of the term of the contract. The parties expected some variance from these predicted capacity factors and these predictions for coal consumption but there was no suggestion that it was expected by either party that the variance would be substantial.

It is clear that the generating unit size and the coal consumption calculations derived from the customary operation of such units were important to plaintiff during the negotiations of this contract. Plaintiff relied on the calculations in conducting its feasibility study, developing a pricing schedule, and designing its mine. Defendants were aware that plaintiff was so utilizing these figures. It is noted that defendants' expert witness testified to the effect that it is a common procedure in the negotiation of such a fuel contract for the public utility or other buyer of coal to calculate the amount of coal expected to be burned and then to communicate such calculations to the coal miner.

Negotiations between defendants and plaintiff were completed by February 3, 1973 and the contract in question was signed April 6, 1973. The contract provides that plaintiff's obligation is to supply the coal requirements for two generating units, each with a capacity of about 350,000 kilowatts net. Plaintiff's sales obligation, however, is not to exceed the mining and delivery of coal sufficient to produce 1830 trillion Btu's over the thirty five year life of the contract. Defendants' purchase obligation is to pay for a yearly quantity of coal, regardless of whether they order that amount. This quantity is a negotiated figure based on a calculation of 85% of the expected coal consumption of the machines. Between these maximum and minimum limits, the contract provides that the actual requirements of the units is to be determinative of the amount of coal ordered and delivered.

It is noted that shortly after the execution of the contract, coal prices began to rise dramatically, due in part to the Arab oil embargo in September of 1973. Prior to that time the price of coal had reflected only a slight upward trend.

Presumably these negotiations and the resulting contract would not have reached this court had the defendants not made two significant decisions in February of 1973 and prior to the execution of the contract. One decision was to build units with a net capacity of 410,000 kilowatts each instead of the 350,000 net capacity specified in the contract. The

other decision was to refrain from communicating to plaintiff any information regarding this increase — at least until some undetermined future date.

Defendants recognized that such an increase in unit capacity, if communicated to plaintiff when the decisions were made, might adversely affect the then status of the contract negotiations. The fuel contract was signed by the parties before the increased size of the units was revealed and at the time of trial, defendants had completed a substantial portion of the construction of these larger sized units.

Plaintiff and defendants draw different conclusions from these facts. Plaintiff contends that the size of the units to be constructed, and “about 350,000 kilowatts” net size described in the contract, was the essential condition of the contract and that defendants abrogated the entire contract by building units of a size larger than that described. Defendants on the other hand, contend that neither the size of the units nor the calculations of estimated coal consumption were essential to this contract and that they should not have been relied upon by plaintiff in its pricing and in its mine design. Defendants assert rather that the maximum and minimum amounts contained in the contract define the obligations of the plaintiff and that construction of units larger than those described in the contract was not, therefore, in breach of the contract. Neither view accurately reflects the evidence nor the controlling law.

I

Both parties to this litigation recognize that the contract in question is a requirements contract. As such, it requires that plaintiff provide and defendants purchase the fuel necessary to operate the generating units described in the contract. It is not, however, a pure requirements contract, but one modified by the maximum seller’s obligation and the minimum buyer’s obligation. It is necessary to this litigation to understand the legal significance of these modifications.

From my reading of the contract, it is clear that one of the effects of the minimum purchase obligation is that plaintiff mine company may at all times require that the defendant utility companies take or pay for the contractual minimum amount of coal regardless of the actual fuel requirements of the generating units. Testimony at trial disclosed that the parties to the contract likewise understand the contract to impose such an obligation on the buyer. There is no suggestion that the defendant purchasers can avoid this obligation, for example, by shutting down their plant or by limiting its operation, even if such a decision is motivated by sound business management.

Such a purchase obligation is a protective provision for the seller and as such eliminates some of the risks for seller which normally attend the

type of requirements contract containing no such minimum purchase obligation. Expert testimony at trial indicated that this type of minimum purchase obligation is becoming a more common feature in coal sales agreements such as the one here in dispute.

Since defendants are thus obligated to purchase a minimum amount of coal, regardless of the actual generating requirements of the units specified in the contract, it follows, in my view, that defendants have the concomitant right to demand delivery of that minimum amount regardless of their actual fuel requirements. The few cases that have dealt with such requirements contracts, all containing similar minimum purchase obligations, have almost unanimously reasoned as we have and have held that the absolute *obligation* to buy a minimum amount necessarily implies the absolute *right* to buy that amount, and that buyer, in demanding delivery of its minimum purchase obligation need not be motivated by the business requirements envisioned by the contract but may, in fact, utilize the commodity completely apart from the operation of the business specified in the contract. See *Magnolia Petroleum Co. v. Farmersville Independent Gin Co.*, 243 S.W. 568 (Tex. Civ. App. 1922); *Corsicana Compress Co. v. Magnolia Petroleum Co.*, 253 S.W. 559 (Tex. Civ. App. 1923); and *Diamond Alkali Co. v. Aetna Explosives Co.*, 264 Pa. 304, 107 A. 711 (1919).

In contrast to the minimum purchase obligation in this contract, the purchase of coal in excess of the contractual minimum is controlled by and dependent upon the actual requirements of the defendants and may be demanded pursuant to those requirements up to the maximum sales limit contained in the contract. More specifically, it is my reading of the contract that it does not give the defendants the right to demand delivery of the contract maximum unless that demand is justified as being required for the actual operation of the two 350,000 kilowatt net machines specified in the contract.

The nature of the negotiations leading up to the execution of this contract is consistent with such an interpretation. All parties recognized that the anticipated unit size was crucial in estimating probable coal consumption and that such estimates were significant to all parties in developing their bargaining positions. Such negotiations would have been meaningless if the parties had not contemplated that the fuel requirements of the generating units would define the purchase and sale obligations above the minimum.

Indeed, since plaintiff and defendants both characterize the contract as a requirements contract it would seem that neither would disagree with this construction of the contract. Both parties have cited the case of *M. W. Kellogg Co. v. Standard Steel Fabricating Co.*, 189 F.2d 629 (10th Cir. 1951) for the proposition that in a requirements contract, the project itself, and the material required to finish that project becomes “the essence of the contract. . . .” 189 F.2d at 631. Nevertheless, the defendants

assert that they have an absolute right to the maximum amount of coal specified in the contract regardless of their actual requirements. Such an assertion is simply not consistent with defendants' own characterization of the contract as being a requirements contract.

Careful consideration has been given to *Diamond Alkali Co.*, *supra*, cited by defendants for the proposition that a buyer in a requirements contract can demand the maximum purchase amount of the contract whether or not it was required in its business. In that case, the contract provided that the seller was obligated to furnish soda ash at a fixed price to the extent of "buyer's entire requirements" within certain maximum and minimum sales limits. The price of soda ash apparently rose and the buyer took advantage of the low contractual price by purchasing in excess of its business requirements and reselling on the open market. The court stated that such transactions did not violate the parties' contract and did not obligate the purchaser to account to the seller for his resale profits. This holding, however, is no more logically consistent than is the position of the defendants in the instant case, in that it also fails to reconcile its conclusion with the fact that the contract was a requirements contract and was so characterized by that court. The opinion does state that the contract was vague as to what purchase requirements were anticipated by the parties to the contract since the nature of the buyer's business could not be detected from the contractual terms. Therefore, the court in *Diamond Alkali Co.* might have viewed the obligations differently had the anticipated purchase requirements been more specifically described in that contract as they are so described in the contract at issue in the instant case.

At any rate, the weight of authority is contrary to this case and to defendants' position. The court in *Staver Carriage Co. v. Park Steel Co.*, 104 F. 200 (7th Cir. 1900) held that any deliveries above the minimum limit in a requirements contract could be demanded only to the extent of the actual business requirements of the purchaser, as those business requirements were contemplated by the parties to the contract. Likewise in *Magnolia Petroleum Co.*, *supra*, the court held that all deliveries in excess of the contractual minimum must be justified by the business requirements of the purchaser.

Finally, in *National Home Products Co. Inc. v. Union Carbide and Carbon Corp.*, 281 App. Div. 604, 121 N.Y.S.2d 130 (1953), *aff.* 306 N.Y. 638, 116 N.E.2d 245 (1953) the court held that minimum and maximum limits in a requirements contract do not transform such a contract into a contract for the sale of a definite quantity. Instead, the court held that such a contract is still a requirements contract obligating the seller to provide the materials necessary to meet the buyer's operational necessities in the business specified by the contract. Unless the contract were given such an interpretation, the court felt that "the 'requirements' provi-

sions of the contracts would seem to be mere surplusage and meaningless." 121 N.Y.S.2d at 132.¹⁴²

It is, therefore, my view that the proper construction of the contract here in question is one that acknowledges the buyer's absolute obligation and its concomitant absolute right to purchase the contract minimum. Additionally, purchases in excess of the minimum limit but less than the maximum must be provided by seller only insofar as they are required by buyer's business operations, as those operations are described in the contract.

We now turn to the question of whether defendants have altered such rights and duties under this contract by departing from the terms of the contract with their construction of generators larger than those specified in the contract.

II

Plaintiff contends that the defendants have abrogated this contract by building generator units substantially larger than anticipated by the parties and larger than specified in the contract. We turn to Colorado law regarding rescission in evaluating this claim.

Under Colorado law, a breach of a contract will not terminate a contract and relieve the other party of its duties thereunder unless that breach is a major breach going to the essential condition of the contract. *Gulick v. A. Robert Strawn & Associates*, 477 P.2d 489 (Colo. App. 1970). Furthermore, the party seeking rescission must show that the injury caused by the breach is irreparable and that more than a mere variance of the contract terms is involved. *Kole v. Parker Yale Development Company*, 536 P.2d 848 (Colo. App. 1975); *Briggs v. Robinson*, 82 Colo. 1, 256 P. 639 (1927).

Colorado law is clear in its requirement that a court exercise caution in terminating a contract. It is widely held, and Colorado is no exception, that forfeitures pursuant to a forfeiture provision in a contract are not looked upon with favor and will be avoided if possible. *Moorman Manufacturing Co. v. Rivera*, 155 Colo. 413, 395 P.2d 4 (1964). *Gulick, supra*, points out that declaring a contract terminated because of a breach in performance is tantamount to declaring such a forfeiture and, therefore, the same caution exercised in declaring a forfeiture was held to be required in terminating a contract. This court has likewise recognized this

142. This is the only case we have found that also holds that the minimum purchase limit in a requirements contract can not be demanded unless it is likewise necessary for the actual business operations of the purchaser. I do not agree with this interpretation of the minimum purchase obligation for the reasons discussed *supra*. It is also noted that this aspect of the court's opinion has been criticized unfavorably. See 54 Colum. L. Rev. 296 (1954).

policy of avoiding contractual forfeitures, *United Buckingham Freight Lines v. Riss & Company*, 241 F. Supp. 861 (D. Colo. 1965), and concludes as the court did in *Gulick* that terminating a contract upon breach of that contract and in the absence of a forfeiture provision should *a fortiori* be avoided if possible.

I recognize that Colorado law generally requires a court to rescind the whole contract and not to affirm or disaffirm the contract in part. *Kelley v. Silver State Savings and Loan Ass'n*, 534 P.2d 326 (Colo. App. 1975); *Tomkins v. Tomkins*, 78 Colo. 574, 243 P. 632 (1926); *Walker v. MacMillan*, 62 Colo. 136, 160 P. 1062 (1916). The Colorado courts, however, have not addressed the question of the partial cancellation of a contract containing separate and divisible obligations. Since that issue is presented by this dispute this court must attempt to predict how a Colorado court would rule if faced with the question of the partial rescission of such a contract. Two facts lead me to believe that Colorado would grant the partial rescission of a divisible contract if the equities require it.

First, the Colorado Supreme Court has held that a court of equity, when declaring the rights and duties under a contract, "should make such adjustment of the case as the facts pleaded and proved will justify." *Cahill v. Readon*, 85 Colo. 9, 15, 273 P. 653, 656 (1928). Such a holding thereby acknowledges that the court in an equitable action must have the necessary flexibility to make a disposition consistent with whatever the equitable requirements of the case may be.

Second, the law from jurisdictions outside Colorado clearly allows the partial rescission of a divisible contract if justice so requires. *See* for example *Reina v. Erassarrett*, 90 Cal. App. 2d 418, 203 P.2d 72 (1949); *Mitzel v. Schatz*, 175 N.W.2d 659 (N.D. Sup. Ct. 1970); *Thompson v. Williams*, 246 S.W.2d 506 (Tex. Civ. App. 1952). *See* also annotation at 148 A.L.R. 417 (1944). I therefore conclude that the partial rescission of a divisible contract would not be inconsistent with Colorado law if such were required for an equitable resolution of a contractual conflict.

In applying the above discussed legal principles to the contract here in question, I find that the contract is divisible in the obligations it imposes on the parties. As pointed out in the previous section, the contract contains an absolute minimum purchase obligation and a requirements purchase obligation for purchases in excess of the minimum. These obligations operate independently of each other and impose obligations of significantly different natures.

I further conclude that the Colorado law governing the possible grounds for rescission justifies the cancelling of only a portion of this contract and that the equities of this case demands such partial rescission. The minimum purchase obligation in this contract, as an absolute obligation, is not influenced by defendants' fuel requirements and is, therefore, equally unaffected by the unit size chosen by defendants. It follows, therefore, that the generating capacities of the units were not a

major factor in either establishing this obligation or in negotiating the particular extent of the obligation. Therefore, even though defendants have breached this contract by constructing larger generating units than specified in the contract, that breach does not go to the essential condition of the contract's minimum purchase obligation. Therefore, under Colorado's stringent rules governing the termination of a contract, defendants' breach does not justify cancelling that portion of the contract.

This breach of performance by defendants, however, does go to the heart of the requirements purchase obligation for amounts of coal in excess of the minimum. As this court concluded above, defendants are entitled to receive coal in amounts in excess of their minimum purchase obligation only if that coal is required by the operation of the generating units specified in the contract. Therefore, in construing this portion of the contract it becomes apparent that the size of the coal consuming units is the essential element in determining the parties' rights and duties thereunder. The contract specified that the generating units would have net capacities of about 350,000 kilowatts each. Defendants, however, are building units with capacities of 410,000 kilowatts net. This increase in size will result in the consumption of an amount of coal substantially in excess of the amount contemplated by plaintiff and in excess of the coal consumption calculations prepared and relied on by both parties during the negotiation of the contract. Defendants should not be allowed to take advantage of this breach, particularly in view of the continuing dramatic rise in the price of coal; this breach is of such a nature as to require rescission of that portion of the contract. Certainly the breach is more than a mere variance of the contractual terms and in it threatens to do irreparable damage to plaintiff. *See Briggs and Kole, supra.*

Defendants, however, point to the rule of law allowing the purchaser in a requirements contract to modify his business operations after the contract is signed and cite *Southwest Natural Gas Co. v. Oklahoma Portland C. Co.*, 102 F.2d 630 (10th Cir. 1939) as authority for that rule. Defendants' reliance on that case is misplaced and entirely inappropriate.

In the case at bar, the purchaser's business requirements specified in the contract were modified prior to the execution of the contract and without notifying plaintiff. In *Southwest*, the improvements made in the business operation of the purchaser were made subsequently to the execution of the contract and were the type of improvements that seller should have anticipated would occur over the life of that contract.

The court in *Southwest* also pointed out that the changes made in purchaser's business were not precluded by the terms of the contract. Defendants in the instant case, however, have made a modification prohibited by the terms of the contract in that the contract specifically stipulates the size of the generating units that were to be built.

Additionally, *Southwest* emphasizes that the modifications were made in good faith and were necessary for the continued efficiency of the

purchaser's plant. Defendants in this action have failed to meet the burden of establishing that their changing the size of the consuming generating units was in good faith. In fact, the evidence strongly suggests to the contrary.

As noted above, this court is aware of the caution that must be exercised in terminating any contractual obligation. The case at bar, however, clearly presents a situation where such an equitable remedy is the only appropriate remedy. A party to a contract may not unilaterally alter the obligations of any of the parties to that contract. Defendants, however, have attempted to increase plaintiff's sales obligation under the requirements portion of this contract by altering their business operations in such a manner as to constitute a material breach of that portion of the contract. Rescission, therefore, is an appropriate remedy. As pointed out, however, the breach does not affect that portion of the contract containing the defendants' minimum purchase obligation and as such, prohibits the termination of that obligation. It is therefore,

ORDERED that

1) Plaintiff must yearly sell to defendants, if defendants so demand, that amount of fuel specified in the "Table for the Minimum Annual Payments" contained in Section 8 of the Craig Station Fuel Agreement, a portion of which is attached hereto as Appendix A.

2) Defendants may purchase, regardless of their operational requirements, that amount of fuel specified in that same Table for Minimum Annual Payments contained in Section 8 of the Craig Station Fuel Agreement.

3) Defendants must make the minimum yearly payments pursuant to the provisions of Section 8 of the Craig Station Fuel Agreement regardless of whether defendants actually receive any coal during that year.

4) Plaintiff is not obligated to furnish to defendants any coal in excess of the above prescribed amounts unless pursuant to a new or supplemental agreement between the plaintiff and defendants.

5) All other provisions of the Craig Station Fuel Agreement, including but not limited to those provisions regarding price, delivery schedules, arbitration, the term of the contract and emergency storage shall remain binding on plaintiff and defendants except insofar as they are modified by this order.

[Appendix A has been omitted.]

**SCHLEGEL MANUFACTURING CO. v.
COOPER'S GLUE FACTORY**

231 N.Y. 459, 132 N.E. 148 (Ct. App. 1921)

Appeal from a judgment of the Appellate Division of the Supreme Court in the first judicial department, entered Dec. 27, 1919, affirming a

judgment in favor of plaintiff entered upon a decision of the court at a Trial Term without a jury.

MCLAUGHLIN, J. Action to recover damages for alleged breach of contract. The complaint alleged that on or about December 9, 1915, the parties entered into a written agreement by which the defendant agreed to sell and deliver to the plaintiff, and the plaintiff agreed to purchase from the defendant, all its "requirements" of special BB glue for the year 1916, at the price of nine cents per pound. It also alleged the terms of payment, the manner in which the glue was to be packed, the place of delivery, the neglect and refusal of defendant to make certain deliveries, the damages sustained, for which judgment was demanded. The answer put in issue the material allegations of the complaint. At the trial a jury was waived and the trial proceeded before the trial justice. At its conclusion he rendered a decision awarding the plaintiff a substantial amount [\$6,431.28]. Judgment was entered upon the decision, from which an appeal was taken to the Appellate Division, first department, where the same was affirmed, two of the justices dissenting. The appeal to this court followed.

I am of the opinion that judgment appealed from should be reversed, upon the ground that the alleged contract, for the breach of which a recovery was had, was invalid since it lacked mutuality. It consisted solely of a letter written by defendant to plaintiff, the material part of which is as follows:

Gentlemen — We are instructed by our Mr. Von Schuckmann to enter your contract for your requirements of "Special BB" glue for the year 1916, price to be 9¢ per lb., terms 2% 20th to 30th of month following purchase. Deliveries, to be made to you as per your orders during the year and quality same as heretofore. Glue to be packed in 500 lb. or 350 lb. barrels and 100 lb. kegs, and your special Label to be carefully pasted on top, bottom and side of each barrel or keg. . . .

Peter Cooper's Glue Factory,
W. D. DONALDSON,
Sales Manager.

At the bottom of the letter the president of the plaintiff wrote: "Accepted, Oscar Schlegel Manufacturing Company," and returned it to the defendant.

The plaintiff, at the time, was engaged in no manufacturing business in which glue was used or required, nor was it then under contract to deliver glue to any third parties at a fixed price or otherwise. It was simply a jobber, selling, among other things, glue to such customers as might be obtained by sending out salesmen to solicit orders therefor. The contract was invalid since a consideration was lacking. Mutual promises or obligations of parties to a contract, either express or necessarily implied, may furnish the requisite consideration. The defect in the alleged contract

here under consideration is that it contains no express consideration, nor are there any mutual promises of the parties to it from which such consideration can be fairly inferred. The plaintiff, it will be observed, did not agree to do or refrain from doing anything. It was not obligated to sell a pound of defendant's glue or to make any effort in that direction. It did not agree not to sell other glue in competition with defendant's. The only obligation assumed by it was to pay nine cents a pound for such glue as it might order. Whether it should order any at all rested entirely with it. If it did not order any glue, then nothing was to be paid. The agreement was not under seal, and, therefore, fell within the rule that a promise not under seal made by one party, with none by the other, is void. Unless both parties to a contract are bound, so that either can sue the other for a breach, neither is bound. (*Grossman v. Schenker*, 206 N.Y. 466; *Levin v. Dietz*, 194 N.Y. 376; *Chicago & Gt. E. Ry. Co. v. Dane*, 43 N.Y. 240; *Hurd v. Gill*, 45 N.Y. 341; *Commercial Wood & Cement Co. v. Northampton Portland Cement Co.*, 115 App. Div. 388; *Jackson v. Alpha Portland Cement Co.*, 122 App. Div. 345; *Crane v. Crane & Co.*, 105 Fed. Rep. 869; *Williston on Contracts*, sec. 104.) Had the plaintiff neglected or refused to order any glue during the year 1916, defendant could not have maintained an action to recover damages against it, because there would have been no breach of the contract. In order to recover damages, a breach had to be shown, and this could not have been established by a mere failure on the part of the plaintiff to order glue, since it had not promised to give such orders.

There are certain contracts in which mutual promises are implied: Thus, where the purchaser, to the knowledge of the seller, has entered into a contract for the resale of the article purchased (*Shipman v. Straitsville Central Mining Co.*, 158 U.S. 356); where the purchaser contracts for his requirements of an article necessary to be used in the business carried on by him (*Wells v. Alexandre*, 130 N.Y. 642); or for all the cans needed in a canning factory (*Dailey Co. v. Clark Can Co.*, 128 Mich. 591); all the lubricating oil for party's own use (*Manhattan Oil Co. v. Richardson Lubricating Co.*, 113 Fed. Rep. 923); all the coal needed for a foundry during a specified time (*Minnesota Lumber Co. v. Whitebreast Coal Co.*, 160 Ill. 85); all the iron required during a certain period in a furnace (*National Furnace Co. v. Keystone Mfg. Co.*, 110 Ill. 427); and all the ice required in a hotel during a certain season (*G. N. Railway Co. v. Witham*, L.R. 9 C.P. 16). In cases of this character, while the quantity of the article contracted to be sold is indefinite, nevertheless there is a certain standard mentioned in the agreement by which such quantity can be determined by an approximately accurate forecast. In the contract here under consideration there is no standard mentioned by which the quantity of glue to be furnished can be determined with any approximate degree of accuracy.

The view above expressed is not in conflict with the authorities cited by

the respondent. Thus, in *N.Y.C. Iron Works Co. v. U.S. Radiator Co.* (174 N.Y. 331), principally relied upon and cited in the prevailing opinion at the Appellate Division, "the defendant bound the plaintiff to deal exclusively in goods to be ordered from it under the contract, and to enlarge and develop the market for the defendant's wares so far as possible."

In *Fuller & Co. v. Schrenk* (58 App. Div. 222; *affd.*, 171 N.Y. 671) the contract provided: "It is hereby agreed that in consideration of W. P. Fuller & Co. buying *all* their supply of German Mirror Plates from the United Bavarian Looking Glass Works, for a period of six months from this date, the said United Bavarian Looking Glass Works" agrees to sell certain mirrors at specified prices. [The discussion of *Wood v. Duff-Gordon*, 222 N.Y. 88, *infra* p. 451, is omitted.]

In *Ehrenworth v. Stuhmer & Co.* (229 N.Y. 210) defendant and its predecessor were desirous of obtaining a market for a particular kind of bread which it manufactured. In order to accomplish this purpose it was agreed that plaintiff should purchase and defendant sell *all* the bread of the kind specified which plaintiff required in a certain locality and pay therefor a price specified in the agreement. The plaintiff also agreed he would not sell any other bread of that kind on that route during the life of the contract, which was to continue so long as the parties remained in business. This contract, it will be noticed, specified the articles to be sold, the price to be paid, the quantity to be furnished, and the term of the contract, during which time plaintiff agreed not to sell any other bread of the kind named in that territory.

In the instant case, as we have already seen, there was no obligation on the part of the plaintiff to sell any of the defendant's glue, to make any effort towards bringing about such sale, or not to sell other glues in competition with it. There is not in the letter a single obligation from which it can fairly be inferred that the plaintiff was to do or refrain from doing anything whatever.

The price of glue having risen during the year 1916 from nine to twenty-four cents per pound, it is quite obvious why orders for glue increased correspondingly. Had the price dropped below nine cents it may fairly be inferred such orders would not have been given. In that case, if the interpretation put upon the agreement be the correct one, plaintiff would not have been liable to the defendant for damages for a breach, since he had not agreed to sell any glue.

The judgments of the Appellate Division¹⁴³ and trial court should be reversed and the complaint dismissed, with costs in all courts.

Hiscock, Ch. J., Hogan, Pound, Crane and Andrews, JJ., concur; Chase, J., deceased.

Judgments reversed, etc.

NOTE

1. In the five years preceding the contract in litigation, plaintiff's orders had never exceeded 35,000 pounds per year. During the 1916 contract period, plaintiff ordered about 170,000 and received 65,000 pounds. Plaintiff tried to fill his 1917 requirement and defendant never repudiated the orders; in fact, defendant's representative promised repeatedly as late as December 1916 that he would ship. 189 A.D. 843, at 846, 179 N.Y.S. 273, at 280. Does the decision amount to saying that jobber's requirement contracts are unenforceable? In the Appellate Division decision, Page, J., in his dissenting opinion had this to say: "The facts in this case show conclusively in my opinion that the plaintiff was not acting in good faith but was using the contract speculatively and not as contemplated by the parties." 189 A.D. 849, 855. Was the promise of defendant's representative not binding?

Why was not the defendant's promise a continuing offer which in turn was accepted?

2. The defendant, a wholesale ice company, agreed to sell to plaintiff coal company 100 tons of ice at a stated price, and plaintiff agreed to purchase all the ice used by it up to 100 tons. Payments were to be made daily and the agreement was to continue for one year. Unknown to defendant, plaintiff at the time of the agreement was not in the ice business and had no use for ice. Two months after the contract was entered into, plaintiff made its first demand for ice to be delivered to a former customer of defendant, who had bought ice until his supply was stopped for failure of payment. Upon defendant's refusal to deliver, plaintiff sued for damages. Held, for defendant. Plaintiff

impliedly represented that it was either in the ice business or would be in the ice business with a market for ice in May or June and would require ice daily not to exceed one hundred (100) tons. It was in no such business and made no bona fide demand for any ice under this contract. In other words, it had no need for ice.

Nassau Supply Company, Inc. v. Ice Service Co., 252 N.Y. 277, 169 N.E. 383 (1929), discussed in 43 Harv. L. Rev. 828 (1930). Comment 2 to U.C.C. §2-306, reprinted *supra* pp. 433-434, requires careful reading.

Section 12. "Instinct with an Obligation"

We have discussed the obligation of good faith on several occasions thus far. We have seen how this obligation has crept into precontractual negotiations, and we have also encountered it in our discussion of re-

quirements and brokerage contracts as well as franchise agreements. In Chapter 4, we shall once again meet the obligation of good faith in connection with insurance contracts.

This section continues the exploration of the notion of good faith in relation to another group of cases. These cases all involve ongoing contractual relations in which one of the two parties appears to be left with a wide discretion about what he must do under the contract. A question is often raised as to whether the scope of discretion is so wide as to render the contract void for want of mutuality. In an effort to safeguard the expectations of those who have entered into a contract, the courts have increasingly imposed a limitation of good faith on the exercise of discretion. In some cases, such a limitation has had the effect of providing a counterpromise where one appeared to be lacking. In other cases, the limitation has entailed a reinterpretation of broadly worded clauses that give one of the parties the right to cancel or make his own obligation conditioned on his satisfaction with the other party's performance. In still other cases, the assertion of a lack of mutuality has been met by judicial manipulation of the consideration doctrine.