

# Contract Law

## In This Unit You Will Find:

**Chapter 4**  
What Is a Contract?

**Chapter 5**  
Elements of a  
Contract

**Chapter 6**  
How Contracts Come  
to an End

.....▶

### Owning Your First Car

This is a big step toward independence but also a big financial and civic responsibility. *What do you think is the most challenging aspect of owning a car?*



## Thematic Project Preview

### Writing a Driving Contract

As you read this unit, use this checklist to prepare for the unit project:

- ✓ List the elements needed to create a contract.
- ✓ Differentiate between classes of contracts.
- ✓ Compare the requirements of an offer and of an acceptance.
- ✓ Explain how offer and acceptance can create contractual rights and duties.
- ✓ Determine whether an agreement is definite enough to be enforced as a contract.

**Legal Portfolio** When you complete the Unit Thematic Project, you will have a real contract to add to your portfolio.



### Research Car Facts

Log on to [glencoe.com](http://glencoe.com) to find resources to help your WebQuest explore the contractual side of having a first car. List your findings in your WebQuest folder to share with your class.



Find Unit 2 study tools such as **Graphic Organizers**, **Academic Skills Review**, and **Practice Tests** at [glencoe.com](http://glencoe.com).

## Ask

### STANDARD & POOR'S

## Investing in Mutual Funds

**Q:** I have heard that mutual funds are a type of investment. What are they?

**A:** A mutual fund is a collective investment that pools money from many investors to buy and sell stocks, bonds, short-term money-market instruments, and other securities traded on stock exchanges around the world. A mutual fund operates by specific rules and while you do not have to sign a contract document, by entering a fund you effectively agree to follow its rules and pay its fees. What the fund invests in is called a portfolio. By law, you should receive a prospectus from the fund company before you invest in it. It tells you the goals of the fund and how it intends to achieve them. You will also find information about the fund's fees.

**Language Arts/Reading** Standard & Poor's is one of the world's main providers of credit ratings and financial-market indices. You can access the S & P Web site through [glencoe.com](http://glencoe.com) and read about the various companies and stocks that mutual funds use as investments.

# What Is a Contract?

## BusinessWeek News

### Bring Your CDs into the iPod Age

By Stephen H. Wildstrom

Copying CDs to computer files isn't difficult. But it is time-consuming—around ten to 15 minutes per disk depending on the speed of your computer, the digital format, and the length of the CDs. If you're like me, it's a task you would cheerfully pay someone else to do.

I tried two different services, Rip Digital and ReadyToPlay, that do the job. They are alike in most respects.

Both charge around \$130 (plus shipping) for the first 100 CDs, with prices dropping as low as \$1 per disk for large quantities. Rip Digital includes a program that automates the process of copying the files from the DVD to your computer and loading the music into your library of iTunes or a musicmatch jukebox.

From now on, every CD I buy goes to the computer immediately to keep the digital library up-to-date. But the ripping services have done the heavy lifting, so now I get to sit back and enjoy the music.

### Flex Your Reading

Efficient critical reading involves being flexible with speed and comprehension. There are several ways of reading critically, and you need to fit a reading style to your needs and to the material.

Go to [glencoe.com](http://glencoe.com) to find Flex Your Reading activities, more information on reading strategies for this chapter, and guided practice in reading contracts (online or printed).





**Legal Download** An interest in music requires building and maintaining your music collection. *When is it legal to download music off the Internet?*

# Agreements and Contracts

## What You'll Learn

- ◆ Explain the nature and importance of contracts.
- ◆ Identify the elements of a valid contract.
- ◆ Analyze the different classes of contracts.
- ◆ Differentiate between express and implied, unilateral and bilateral, and oral and written contracts.

## Why It's Important

Knowing the elements and characteristics of a contract will help you determine whether an agreement is valid or not.

## Academic Standards

Reading and completing the activities in this section will help you practice the following academic standards:

### Math (NCTM CS2 3)

Recognize and apply mathematics in contexts outside of mathematics. Solve problems that arise in mathematics and in other contexts.

### English Language Arts (NCTE 6)

Apply knowledge of language structure, language conventions, media techniques, figurative language, and genre to create, critique, and discuss print and non-print texts.

## Reading Guide



### Before You Read

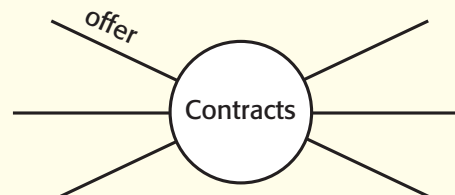
**Connect** If you have ever agreed to conditions to enter a Web site, you have made a contract. What are some contracts you have made lately?

### Focus on Ideas

For a contract to be valid, it must meet several requirements and have certain characteristics.

### Take Notes

Create a graph like the one shown and use it to take notes as you read this section. Go to [glencoe.com](http://glencoe.com) to find graphic organizers and tips on how to improve your note-taking skills.



The Six Components of a Contract



### Key Terms

You will learn these legal words and expressions in this chapter. You can also find these terms in *Black's Law Dictionary* or in an online legal dictionary.

- contract
- offer
- acceptance
- genuine agreement
- express contract
- implied contract
- bilateral contract
- unilateral contract



### Academic Vocabulary

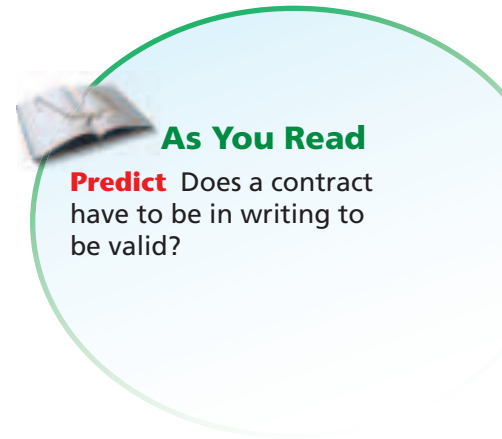
You will find these words in your readings and in your tests. Look them up in a dictionary and familiarize yourself with them.

- determine
- assume
- require

## Understanding Contract Law

*Do you think a contract always is a written document that needs to be signed?*

If you bought your first car last year or sold your old video games at a garage sale, you might know that these activities involve contracts. Many common daily activities also involve contracts, from buying a fast food meal to filling your car with gas. Most people think a contract is a long, printed, formal document that they sign when buying a vehicle, selling their house, or purchasing insurance. Such formal documents represent only a small fraction of the contracts that you will make in your lifetime. The truth is that you create a contract any time you agree to exchange things of value.



### As You Read

**Predict** Does a contract have to be in writing to be valid?

**“I guess it is easy being green.”**

Presenting the 36 mpg Ford Escape Hybrid, the most fuel-efficient SUV on Earth.\* How green is that?  
[www.fordvehicles.com](http://www.fordvehicles.com)

ESCAPE HYBRID

\*Based on 2007 EPA Fuel Economy Guide and 11.2 EPA 36MPG estimated city mpg. 27 mpg highway, 27MPG. Actual mileage will vary. © The McGraw-Hill Companies, LLC. All Rights Reserved.



### Contracts Are Everywhere

Contractual agreements are not always obvious, but they are everywhere in our lives. *Do you think Ford’s claim of 36 miles per gallon gas consumption is a contract? Why or why not? When you have finished reading and studying this chapter, look at this ad again. Would you change your original answer? Explain how and why?*

**Research Car Facts**

A teen driver-family agreement is a form of contract. Log on to [glencoe.com](http://glencoe.com) to find WebQuest resources, research key issues, and continue your WebQuest project.

*List your findings in your WebQuest folder to share with your class.*

**Vocabulary** You can find vocabulary definitions in the **Key Terms** glossary and **Academic Vocabulary** glossary in the back of this book.

## The Nature of a Contract

*Are all agreements you make contracts?*

A **contract** is any agreement enforceable by law. You should never enter into a contract without understanding the legal responsibilities involved. Not all agreements are contracts. An informal promise to take out the trash is not a contract. In contrast, an ad in a newspaper offering a reward for a lost skateboard is a type of contract. If someone answers the ad and returns the skateboard, the person who placed the ad will owe the person who returned the skateboard what was promised as a reward in the ad.

### The Three Theories of Contract Law

The legal responsibilities associated with contracts are based on what the parties involved do and say to one another. In the past, courts asked whether the parties to a contract exchanged things of equal value. This was called the equity theory of contract law. As industrial capitalism developed, the courts focused on the exercise of each party's will: they asked whether the parties really had agreed to the terms of an agreement. This was called the will theory of contract law. But, it was still very difficult to **determine** what the parties were thinking as they had entered into an agreement. The courts tried to determine if the parties had reached a meeting of the minds and, gradually, this led to a search for elements that consistently appeared in genuine agreements. The courts focused on the form of agreements. This became known as the formalist theory of contract law.

### The Elements of a Contract

The six elements of a contract, as shown in **Figure 4.1**, are offer, acceptance, genuine agreement, consideration, capacity, and legality. To be legally complete, a contract must include all six elements. Notice that the list does not include anything written. Not all contracts have to be in writing to be enforceable.

An **offer** is a proposal by one party to another intended to create a legally binding agreement. An **acceptance** is the second party's unqualified willingness to go along with the first party's proposal. A **genuine agreement** means that an agreement is true and genuine: a valid offer is met by a valid acceptance. Circumstances such as fraud, misrepresentation, mistake, undue influence, and economic duress can destroy the genuineness of an agreement. The fourth element, capacity, is the legal ability to enter a contract. The law generally assumes that anyone entering a contract has the capacity, but this assumption can be disputed. The fifth element, consideration, is the exchange of things of value. In an offer to let someone borrow a car, there is no consideration in the agreement if nothing is offered in return. People cannot enter into contracts that include illegal acts. Legality, the sixth element, means that the contract does not entail violating any laws.

## Figure 4.1 Elements of a Contract

**Capacity** The law presumes that anyone entering a contract has the legal capacity to do so. Minors are generally excused from contractual responsibility, as are mentally impaired people and individuals under the influence of drugs or alcohol.

**Consideration** Consideration is the thing of value promised to one party in a contract in exchange for something else of value promised by the other party. The mutual exchange binds the parties together.

**Legality** Parties are not allowed to enforce contracts that involve illegal acts. Some illegal contracts involve agreements to commit a crime or a tort. Others involve activities made illegal by statutory law.




**Offer** A proposal made by one party (the offeror) to another party (the offeree) indicating a willingness to contract.



**Acceptance** The agreement of the offeree to be bound by the terms of the offer.



**Genuine Agreement** Offer and acceptance go together to create genuine agreement or a meeting of the minds. Agreement can be destroyed by fraud, misrepresentation, mistake, duress, or undue influence.

 An agreement is not a contract unless it contains the six elements of a contract.  
*Of the six elements, which is the most crucial to setting up a valid contract?*



## Reading Check

**Enumerate** How many elements does a contract need to be complete?

## Characteristics of a Contract

Now that you know about the different elements of a contract, can you think of different types of contracts?

Contracts can be created in different ways and can **assume** diverse forms. A contract can be described by any of the following characteristics:

- valid, void, voidable, or unenforceable
- express or implied
- bilateral or unilateral
- oral or written

Any contract can have characteristics from one or more of these four groups. That is, a contract can be valid, express, bilateral, and written. Let's take a closer look at what these characteristics indicate about a contract.

### Valid, Void, Voidable, or Unenforceable Contracts

The word valid means legally good, thus a valid contract is one that is legally binding. On the other hand, a contract that is void has no legal effect. An agreement that is missing one of the previously discussed elements would be void, such as any agreement to do something illegal.

When a party to a contract is able to void or cancel a contract for some legal reason, it is a voidable contract. It is not void in

## Case Study – Vokes v. Arthur Murray

**Critical Thinking** Who do you think should win this case? Why?

**Flex Your Reading**

Note key facts in the text below and look up words you do not understand. Restate difficult ideas in your own words. Go back and reread the text quickly to make sure you did not miss any important detail. Now, you are ready to formulate an opinion.

**Misled into a Contract?** Audrey Vokes went to a dance party offered by the Arthur Murray, Inc., dancing school, where she was persuaded to sign a contract for a dance course. Ms. Vokes was told she was an excellent dancer with grace and poise, and was encouraged to take more dance lessons. She was repeatedly talked into taking more dance courses by assurances that she was rapidly improving and developing in her dancing skills, and that additional lessons would make her a beautiful dancer, capable of dancing with the most accomplished dancers. Over a period of 16 months, Ms. Vokes took a total of 14 dance courses at a cost of over \$31,000. In fact, Ms. Vokes had no skill as a dancer and her dancing did not improve with lessons. When she finally realized this, she sued the Arthur Murray dance school, claiming it had misled her to get her to sign a contract.

*Vokes v. Arthur Murray, Inc., 212 So.2d 906 (FL)*



Go to [glencoe.com](http://glencoe.com) for more case study practice.

itself but may be voided by one or more of the parties. A contract between two minors could be voidable by either of them because minors have the right to get out of contracts (see Chapter 5).

An unenforceable contract is one the court will not uphold, generally because of some rule of law, such as the statute of limitations. If you wait too long to bring a lawsuit for breach of contract, the statute of limitations may have run its course, making the contract unenforceable.

## Express or Implied Contracts

An **express contract** is a contract statement that may be oral or written. An **implied contract** is a contract that comes about from the actions of the parties. People often enter into implied contracts without exchanging a single word.

**Example** Herb Schneider went to a self-service gas station that requires payment before the attendant will turn on the pumps. He handed the attendant \$10, returned to his car, pumped \$10 worth of gas into his tank, and drove off. Neither party spoke a single word, yet an implied contract arose from their actions.

## Bilateral or Unilateral Contracts

Another characteristic of a contract to consider is whether it is bilateral or unilateral. See **Figure 4.2** for a visual representation of bilateral and unilateral contracts. A **bilateral contract** is a contract that contains two promises. One party promises to do something in exchange for the other's promise to do something else. Most contracts are created this way.

A **unilateral contract** is a contract that contains a promise by only one person to do something, if and when the other party performs some act. If your friend



**Bilateral:** *adj* Affecting two sides or parties. From Latin *bilateralis*; *bi* = two + *latus* = side: having two sides.

**Unilateral:** *adj* Done or undertaken by one person or party. From Latin *unus* = one + *latus* = side: having one side.

**Vocabulary Builder** List and define five words that begin with the prefix *bi* or with the prefix *uni*.

**Look It Up!** Check definitions in *Black's Law Dictionary* or an online glossary. For direct links, go to [glencoe.com](http://glencoe.com) to find more vocabulary resources.



A contract may be unilateral or bilateral. *In which type of contract do both parties, the offeror and the offeree, make promises?*

says, “I’ll sell you my DVD player for \$150 if you give me the cash before noon tomorrow,” he or she will not be **required** to keep the promise unless you hand over the cash before noon on the following day.

A reward offer is one of the most common instances of a unilateral contract. The acceptance of the reward offer must precisely comply with the offer.

**Example** Anne Chen placed an ad in the local newspaper offering a reward for the return of her lost laptop computer. Ms. Chen’s offer of a reward alone did not create a contract. The contract would come into existence only when someone returns the laptop. Ms. Chen would then owe the finder the reward.

### After You Read

**Summarize** List the components of a legal contract.

## Oral or Written Contracts

An oral contract is created by word of mouth and comes into existence when two or more people form a contract by speaking to each other. One person usually offers to do something, and the other party agrees to do something else in return. Most contracts are oral contracts of this nature.

Sometimes, however, it is desirable to put contracts in writing. A written contract assures that both parties know the exact terms of the contract and also provides proof that the agreement was made. A law, the Statute of Frauds, requires that certain contracts must be in writing to be enforceable.

## SECTION 4.1 ASSESSMENT

### Self Check

1. What are the differences among valid, void, and voidable contracts?
2. What are the differences between express and implied contracts?
3. What is a unilateral contract?

### Academic Connection

**Mathematics** You recently borrowed \$500 from a friend. You signed a contract that requires you to pay back one third of the loan every month for three months. How much will you

have to pay back each of the first two months? How much will you have to pay back the third month?

**CONCEPT** **Number and Operations: Using Fractions, Decimals, and Rounding** To figure out  $\frac{1}{3}$  of \$500, divide 500 by 3 and round to the nearest cent. Remember to round numbers of 5 or more up and numbers less than 5 down. For example, \$2.224 rounds to \$2.22 and \$2.226 rounds to \$2.23. To get the payment for the third month, subtract the

amounts for the first two months from 500.



For more math practice, go to the Math Appendix.

### Critical Thinking

#### Reward: Lost Backpack

You lost your backpack and posted a \$20 reward for it. If someone who did not know about the reward returned the backpack, would you be legally obligated to pay the reward?



Go to [glencoe.com](http://glencoe.com) to check your answers.

# How a Contract Begins

## SECTION 4.2

### Reading Guide



#### Before You Read

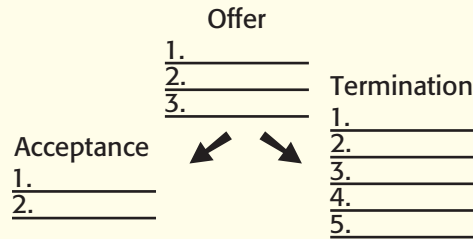
**Connect** Businesses make offers to potential customers using a variety of methods. What are some ways you have received offers?

#### Focus on Ideas

A contract begins with a clear offer, which can be either accepted, changed, or terminated.

#### Take Notes

Create a graph like the one shown and use it to take notes as you read this section. Go to [glencoe.com](http://glencoe.com) for tips on how to improve your note-taking skills.



#### Key Terms

You will learn these legal words and expressions in this chapter. You can also find these terms in *Black's Law Dictionary* or in an online legal dictionary.

- invitations to negotiate
- mirror image rule
- counteroffer
- revocation
- rejection



#### Academic Vocabulary

You will find these words in your readings and in your tests. Look them up in a dictionary and familiarize yourself with them.

- definite
- specify
- impose

### What You'll Learn

- ◆ Explain the requirements of a valid offer.
- ◆ Recognize the requirements of an acceptance.
- ◆ Distinguish the differences between an offer, an invitation to negotiate, an acceptance, and a counteroffer.
- ◆ Explain how offers are terminated.

### Why It's Important

You need to know when an offer has been made and accepted for a contract to go into effect.

### Academic Standards

Reading and completing the activities in this section will help you practice the following academic standards:

**English Language Arts (NCTE 9)** Develop an understanding of and respect for diversity in language use, patterns, and dialects across cultures, ethnic groups, geographic regions, and social roles.

**English Language Arts (NCTE 6)** Apply knowledge of language structure, language conventions, media techniques, figurative language, and genre to create, critique, and discuss print and non-print texts.



The courts consider some advertisements as offers when they contain specific promises, use phrases such as “first come, first served,” or limit the number of items that will be sold. In such cases, under the terms of the advertisement, the number of people who can buy the product becomes limited, making the advertisement an offer rather than an invitation to negotiate.

Price tags, signs in store windows and on counters, and prices marked on merchandise are treated as invitations to negotiate rather than as offers.

## Definiteness and Certainty

An offer must be **definite** and certain to be enforceable. A landlord of an apartment with faulty plumbing might agree to pay a share of the cost if the tenant fixes the plumbing, but the court would not enforce the contract because it was not possible to determine what the parties meant by a share.

**Vocabulary** You can find vocabulary definitions in the **Key Terms** glossary and **Academic Vocabulary** glossary in the back of this book.

## Communication to the Offeree

Offers may be made by telephone, letter, telegram, fax, e-mail, or by any other method that communicates the offer to the offeree.

## Requirements of an Acceptance

*How can you tell if an offer has been accepted?*

The second element of a legally binding contract is acceptance of the offer by the offeree. As in the case of an offer, certain basic requirements must be met: the acceptance must be unconditional and must follow the rules regarding the method of acceptance.



### **American Airlines, Inc. v. FareChase, Inc.**

*Case No. 067-194022-02 (Texas, 67th Dist., Mar. 8, 2003).*

FareChase, Inc., is a search engine whose customers are travel agencies. Its software scours—or scrapes—the Web sites of airlines, hotels, and car rental agencies to find the best rates. In February, 2003, American Airlines (AA) won an injunction against FareChase, alleging that FareChase scraped AA’s site and took information without its permission. AA also claimed that FareChase violated the law of “trespass to chattels”—or interfering with someone’s ownership of goods. Even though AA’s Web site, AA.com, is a public site, its home page contains a statement restricting the use of the information on its site.

### **Ruling and Resolution**

FareChase appealed the ruling on the grounds that the statement on AA’s home page used a shrinkwrap or browsewrap agreement, which unfairly limits the use of facts. AA eventually settled with FareChase. According to the settlement, AA agreed to let FareChase search its site with some restrictions.

**Critical Thinking** Did FareChase have any type of contract with American Airlines? Do you think that FareChase did need a contract allowing the search of a public Web site? Why or why not?

## Unconditional Acceptance

The acceptance must not change the terms of the original offer in any way according to the mirror image rule. **The mirror image rule means that the terms stated in the acceptance must exactly mirror or match the terms of the offer.** Any change in the terms of the offer means the offeree has not really accepted the offer but has made a counteroffer. **A counteroffer is a response to an offer in which the terms of the original offer are changed.** In that case, the original offeror is not obligated to go along, and no contract results. Instead, the offeror becomes an offeree and may accept or reject the counteroffer.

Contracts for the sale of goods are exceptions to the mirror image rule. These exceptions include contracts for personal property such as clothing, furniture, food, motor vehicles, appliances, and other items. The primary exceptions are created by the Uniform Commercial Code (UCC), which is a set of statutes that covers the law of sales as well as other areas of commercial law. It was drafted to make trade among the states easier and has been adopted with minor variations by 49 states. Only Louisiana has not adopted all of its provisions.

## Methods of Acceptance

The time at which an acceptance takes place is important because that is when the contract comes into existence. When the parties are dealing face-to-face or on the telephone, no special problem exists. One party speaks, and the other listens and communicates the offer or the acceptance.

Special rules, however, govern acceptances that take place when the parties are separated by a distance and must communicate by letters, telegrams, or fax. According to common law, an acceptance that must be sent over long distances is effective when it is sent. Any method of communication that has been expressly or impliedly endorsed by the offeror would qualify. Common law also says that an acceptance is implied when the offeree accepts by the same or a faster means than that used by the offeror.

The authorization of an acceptance can also be implied by any reasonable means, including past practices between the parties, the usual method in the trade, or the customary means in comparable transactions. Naturally, the offeree must correctly address the acceptance so that it is delivered to the right place. If the address is faulty, the acceptance is not complete until delivery has been made to the offeror. It is also possible for the offeror to **specify** the time by which the acceptance must be received to be effective.


This rule applies to contracts for real estate and services. For sale-of-goods contracts under the UCC, the acceptance takes place when it is sent, as long as the method of communication is reasonable. Consequently, the acceptance of a mailed offer for goods would be effective when it is sent electronically, via fax, or through an overnight carrier. If the offeror states in the offer what method the offeree must use to accept, that method must be followed.

### Reading Check

**Explain** What are the characteristics of an offer?





 **Long Distance Acceptance** Problems may arise when the acceptance of a contract must travel over long distances. *How can people make certain that an acceptance is valid and effective when it must travel to a distant location?*

Sometimes, an offer specifies that it must be accepted by an action. In these cases, the action must take place before there is an acceptance. The offeror cannot **impose** silence on the offeree as the means of acceptance unless he or she has previously agreed to this condition or has allowed silence to signal acceptance in the past. In contrast, if the offeror has established silence as the means of acceptance, then he or she will have to live by that condition if the offeree accepts by remaining silent.

## Termination of an Offer

*Can you change your mind and withdraw an offer?*

Even though an offer has been properly communicated to the offeree, it may be terminated. This termination may occur in any of five ways: revocation, rejection, counteroffer, expiration of time, and death or insanity.

### Revocation

**Revocation** is the taking back of an offer by the offeror.

The offeror has a change of mind or circumstances and decides to withdraw the offer before it has been accepted. Two important rules govern revocation: an offer can be revoked any time before it is accepted, and a revocation becomes effective when it is received by or communicated to the offeree.





# Global Law

## Entering Contracts in China

In the United States, a signed contract means that all parties know who will do what, with what level of quality, and by what deadline. Once the contract is signed, the parties move on to fulfill the contract, knowing that everyone will do their part. These rules do not exist in China. When people sign a contract there, they simply agree that they want to do business with one another, that the goals of the contract are desirable, and that the terms of the contract are reasonable. However, everyone knows that activities do not always happen as planned.

Camille Schuster, a consultant, speaker, and professor of marketing, international negotiations, and consumer-centered business practices, gives these guidelines for conducting business and managing contracts in China:

- 1 Maintain frequent, regular communication.
- 2 Asking “yes” or “no” questions will not generate useful information. You will be spared embarrassment, you will feel reassured, and you will know nothing. Instead of asking your Chinese contact if the production deadline will be met, try

asking about significant events in the production process during the past week or month, or to describe recent activities of members of the production team.

- 3 Meet face-to-face. This is a relationship culture that requires personal, one-to-one commitment.
- 4 Represent all levels. Chinese culture is hierarchical and communication serves to preserve harmony. Problems are not freely discussed with superiors. Your team needs to include people at different levels of the hierarchy so that quality-control managers talk with other quality-control managers, and line engineers talk with other line engineers.

### Across Cultures: The Importance of Guanxi

**Guanxi** (*gwan-shee*) means relationships. In the Chinese business world, personal connections are the basis for most business deals and contracts. It is very common for employees from one company to visit the residence of acquaintances from other organizations and bring gifts.

**Critical Thinking:** *What key contractual components are not included in Chinese contracts?*

## Rejection

**Rejection** is a refusal of an offer by the offeree that brings the offer to an end. For example, if someone says to you, “I’ll sell you my camera for \$150,” and you say, “I don’t want it,” then the offer has come to an end.

## Counteroffer

A counteroffer ends the first offer. If someone says to you, “I’ll sell you my camera for \$50,” and you say, “I’ll give you \$35 for it,” no contract comes into existence unless the original offeror accepts your new offer. If you later say, “Okay, I’ll give you \$50 for the camera,” you will be making a new offer, which the original offeror may accept or reject.

## Expiration of Time

If the offeror sets a time limit for the acceptance of the offer, it must be honored. Assume that Bradley has offered to sell Franz his motorcycle for \$1,745. Bradley tells Franz the offer will remain

open until noon of the following day. To create the contract, Franz must accept within that time period.

If no time for acceptance is stated in the offer, it must be accepted within a reasonable time. Otherwise, no contract exists. What is a reasonable time depends on the circumstances. For example, a reasonable time to accept an offer for purchasing a truckload of ripe tomatoes would be different from a reasonable time to accept an offer for purchasing a house.

When an offeree pays money or other consideration to an offeror to hold an offer open for an agreed period of time, an option contract comes into existence. An option is a binding promise to hold an offer open for a specified period of time. It offers to the holder of the option the exclusive right to accept the offer within the agreed time, subject to the terms of the option. For example, you might offer a seller \$50 to hold an offer open for two days. Such a contract is legally binding. For an entire contract to be completed, the option must be exercised by the person holding the option. This requires an absolute, unconditional, unqualified acceptance exactly according to the terms of the option.

## Death or Insanity

If the offeror dies or becomes insane before the offer is accepted, the offer comes to an end. Although death ends an offer, it does not end a contract, except for contracts related to personal services.



### After You Read

**Summarize** List the key requirements of an offer and of an acceptance.

## SECTION 4.2 ASSESSMENT

### Self Check

1. What are the requirements of an offer?
2. What are the requirements of an acceptance?
3. When is an offer terminated?

### Academic Connection

#### English Language Arts

Now that you have learned why contracts are so important in business life, imagine that you work as

an executive manager for a company that outsources the manufacturing of electrical components to a company in China. Make sure you read the Global Law feature on page 92 and research contractual and communication issues between U.S. and Chinese businesses. Draft an e-mail memo addressed to the five mid-level production and marketing managers who have been asked to travel to China next month to make sure component production

is going according to plan. Outline specific instructions and general advice on how to handle potential problems during the upcoming trip. Make sure your e-mail follows appropriate memo format.

### Critical Thinking

#### Identifying an Offer

Why is it important to be able to distinguish between an offer and an invitation to negotiate?



Go to [glencoe.com](http://glencoe.com) to check your answers.

# Chapter 4 Review and Assessment

## Summary

### Section 4.1 Agreements and Contracts

- ◆ A contract is any agreement enforceable by law. The six elements of a contract are: offer, acceptance, genuine agreement, consideration, capacity, and legality.
- ◆ Valid contracts are legally binding. A void contract has no legal effect because at least one element is missing. A contract may be voided by one of the parties because of a defect.
- ◆ An express contract is stated in words. It may be written or oral. An implied contract is implied from the actions of the parties.
- ◆ Bilateral contracts are formed by promises that parties make to each other. A unilateral contract contains one party's promise that it will fulfill if and when the other party performs an act.
- ◆ Oral contracts are created when a party verbalizes a promise and the other party responds with a spoken promise. A written contract contains the promises in writing.

### Section 4.2 How a Contract Begins

- ◆ An offer is a proposal by one party to another party to enter a contract. An offer must be (1) seriously intended, (2) definite and certain, and (3) communicated to the offeree.
- ◆ An invitation to negotiate may look like an offer, but it is not. Any such invitation cannot be made into an offer by agreeing to the terms of the invitation.
- ◆ An acceptance must meet two requirements: (1) it must be unconditional; and (2) it must follow the rules regarding the method of acceptance. Unconditional acceptances do not seek to change the terms of the original offer in any way.
- ◆ An offer must be accepted without change to its terms. If an offeree changes the terms of an offer, this is not an acceptance, but a counteroffer which the original offeree then may choose to accept or reject.
- ◆ An offer is terminated by revocation, rejection, counteroffer, expiration of time, death, or insanity.

## Vocabulary Builder

1 On a sheet of paper, use each of these terms in a sentence.

### Key Terms

- contract
- offer
- acceptance
- genuine agreement
- express contract
- implied contract
- bilateral contract
- unilateral contract
- invitations to negotiate
- mirror image rule
- counteroffer
- revocation
- rejection

### Academic Vocabulary

- determine
- assume
- require
- definite
- specify
- impose



Go to [glencoe.com](http://glencoe.com) to play a game and improve your legal vocabulary.

**Key Points Review**

Answer the following questions. Refer to the chapter for additional reinforcement.

- 2 Describe the formalist theory of contract law.
- 3 Explain the elements of legal contracts.
- 4 What are the exceptions to the mirror image rule?
- 5 When an acceptance is sent over a long distance, when does it become effective?
- 6 Under what circumstances is a contract voidable?
- 7 Why is it desirable to put some contracts in writing?
- 8 What two rules govern the revocation of contracts?
- 9 Explain the differences between bilateral and unilateral contracts.

**Standardized Test Practice**

- 10 Read this excerpt of the Uniform Commercial Code (UCC) and complete questions 1 and 2.

**§ 1-103. Construction of UCC to Promote its Purposes and Policies: Applicability of Supplemental Principles of Law.**

The UCC must be liberally construed and applied to promote its underlying purposes and policies, which are: (1) to simplify, clarify, and modernize the law governing commercial transactions; (2) to permit the continued expansion of commercial practices through custom, usage, and agreement of the parties; and (3) to make uniform the law among the various jurisdictions.

**§ 1-105. Severability.**

If any provision or clause of the UCC or its application to any person or circumstance is held invalid, the invalidity does not affect other provisions or applications of the UCC which can be given effect without the invalid provision or application, and to this end the provisions of the UCC are severable.

**1. The purpose of the UCC is to**

- A simplify criminal law
- B simplify and bring up-to-date the law that rules commercial transactions
- C create different rules for different jurisdictions
- D none of the above

**2. The UCC section 1-105 on severability means that**

- A if one section of the UCC does not apply to a case, all sections of the UCC are invalid
- B if a UCC provision does not apply, it can be severed and other provisions remain valid
- C no provision or clause can ever be severed, or set aside, from the UCC
- D all of the above

**Test-Taking Strategies**

Read the stem of the statement carefully, then read each of the answer options all the way through.



## Apply and Debate

Read the following scenarios. Get together with other students in pairs or groups of three and take a position on each scenario. Debate your position in class with students taking the opposite position or prepare a written argument justifying your position.

### 11 Twin Pines

The Galaxy Research Center e-mailed an offer to the owners of Twin Pines, a farm in rural Arkansas. The e-mail message stated: "Please consider this our offer to purchase between 9,000 and 11,000 acres of your 15,000-acre tract of farmland near Twin Pines, Arkansas. Our offering price is between \$15,000 and \$19,000 per acre. Respond ASAP."

**You Debate** *Is this e-mail message a legally effective offer? Why or why not?*

### 12 Homecoming

Connie Adler agreed to go to the homecoming dance with Fred Wolfe. Later, Steve McNamara, the captain of the football team, asked Connie to be his date for homecoming. Connie broke her date with Fred to go to the dance with Steve.

**You Debate** *Does Fred have a legal claim against Connie? Why or why not?*

### 13 Pocket Calculator

Bob Goodman made a verbal agreement to buy a pocket calculator from Howard Hermann for \$35. When Hermann delivered the calculator, Goodman refused to accept it, stating that he was not bound by his verbal agreement.

**You Debate** *Was Goodman correct? Why or why not?*

### 14 Waterbeds

Home Furniture Company advertised its waterbeds in a local newspaper. The newspaper mistakenly advertised the beds for \$49 instead of \$249.

**You Debate** *Must Home Furniture sell the beds at the advertised price? Defend your position by citing which legal principle is involved and how it applies.*

### 15 Revocation

Victor Archer mailed an offer to Sally Miles. Sally mailed a properly addressed and stamped letter of acceptance ten minutes before she received a revocation from Victor.

**You Debate** *Was the revocation effective? Defend your position by citing which legal principle is involved and how it applies.*





## Case Study Practice – Heiman v. Parrish



**16 Is an Agreement a Contract?** In August of 1994, Jerod Heiman purchased a \$9,033 diamond engagement ring. He then asked Heather Parrish to marry him. She said yes and took the ring. About a year later, in October 1995, Mr. Heiman broke off the engagement. Mr. Heiman asked Ms. Parrish to return the ring to him, but she refused. Mr. Heiman then sued her to retrieve the ring.

Ms. Parrish argued to the court that an engagement ring is a part of a contract between two parties to get married at a later date. She argued that Mr. Heiman broke off the engagement, breached the contract, and could not recover the ring.

Mr. Heiman argued that the proposal and engagement were not a binding contract but rather a statement that the parties would get married. The ring was a conditional gift to Ms. Parrish, which Ms. Parrish could keep if the two got married. Since the two did not get married, Mr. Heiman had a right to recover the ring.

*Source: Heiman v. Parrish, 942 P.2d 631 (Kan. 1997)*

**Practice** Was there a contract between Mr. Heiman and Ms. Parrish?

## 17 Ethics Application

**Reward or Not?** Suppose you posted a reward notice that read, “Reward: \$50 for the return of my lost iPod.” Someone who did not know about the reward offer found your iPod and returned it to you.

- ◆ Would it be legal not to pay the reward money to the person who returned your iPod? Explain.
- ◆ Would it be ethical not to pay the reward money? Explain.

## 18 Internet Application

**Find out About Contracts** A youth group to which you belong plans to build a teen activity center. You and other members of the group are in charge of researching what the key contractual issues would be between the youth group and a contractor and how to go about writing a contract draft.



Go to [glencoe.com](http://glencoe.com) to access the Web site sponsored by QuickForm Contracts and follow the instructions for the drafting of a hypothetical contract.



## Reading Connection

**Outside Reading** Go to [glencoe.com](http://glencoe.com) for a list of reading suggestions about contracts.

# Elements of a Contract

## BusinessWeek News

### Harry Potter and the Cyberpirates

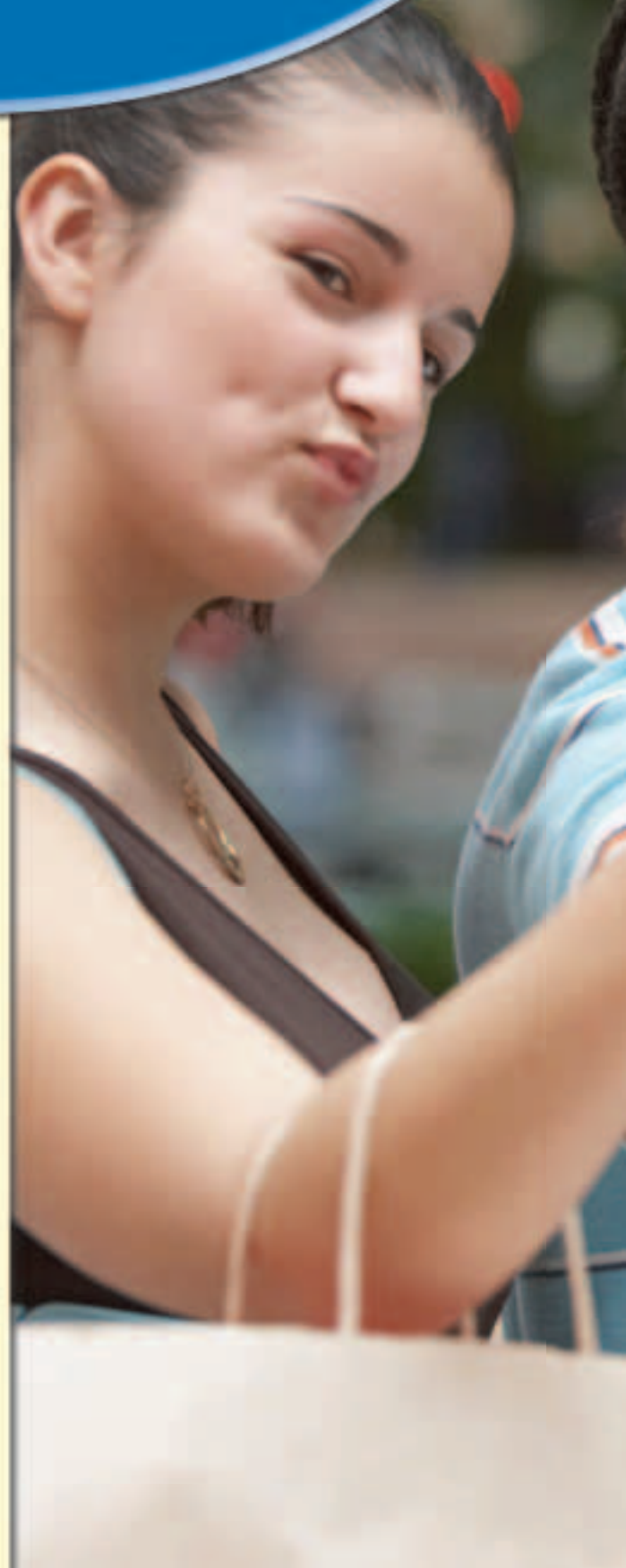
By Mira Serrill-Robins

Sales of *Harry Potter and the Half-Blood Prince*, the sixth book in J.K. Rowling's series, are scorching: More than 8.9 million copies moved in the first 24 hours of publication in the U.S. and Britain. But those are just the legal copies. Pirated electronic versions also are hot, with copying more frenzied than for any of the previous five Potter books. About 15,000 text and audio versions were downloaded during the first three days of release, says Web market-research firm BigChampagne. That's a remarkable pace for books, which aren't as popular with e-pirates as music or movies. Moreover, in this case, pirates had to scan 672 pages. BigChampagne found numerous links, including several attached to files using the free BitTorrent file-sharing program. One site turned up 258 items when the term *Harry Potter* was searched. Rowling, who hasn't OK'd electronic versions of her books, may have to conjure an anti copying spell.

### Flex Your Reading

Efficient critical reading involves being flexible with speed and comprehension. There are several ways of reading critically, and you need to fit a reading style to your needs and to the material.

Go to [glencoe.com](http://glencoe.com) for Flex Your Reading activities, more information on reading strategies for this chapter, and guided practice in reading contracts.





**Minors and Contracts** Suppose you need to purchase a cell phone. *If you are under 18, can you sign an agreement, such as a wireless phone contract?*



## What You'll Learn

- ◆ Assess contractual capacity.
- ◆ Explain the statute of frauds and the parol evidence rule.
- ◆ List minors' contractual rights and responsibilities.
- ◆ Define legality and illegality.

## Why It's Important

Understanding legality and capacity will enable you to assess and interpret contracts correctly.

## Academic Standards

Reading and completing the activities in this section will help you practice the following academic standards:

**Social Studies (NCSS 2)** Study the ways human beings view themselves in and over time.

**Math (NCTM PSS2)** Solve problems that arise in mathematics and in other contexts.

## Reading Guide



## Before You Read

**Connect** Does everybody have the same right to enter into any type of contract?

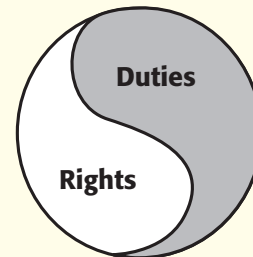
## Focus on Ideas

Specific rules govern who can enter into contracts and whether a contract is legal, valid, or void.

## Take Notes

Create a graph like the one shown and use it to take notes as you read this section. Go to [glencoe.com](http://glencoe.com) to find graphic organizers and tips on how to improve your note-taking skills.

## Contractual Rights and Duties of Minors



## Key Terms

You will learn these legal words and expressions in this chapter. You can also find these terms in *Black's Law Dictionary* or in an online legal dictionary.

- capacity
- minor
- majority
- emancipated
- disaffirm
- ratification
- public policy
- Statute of Frauds



## Academic Vocabulary

You will find these words in your readings and in your tests. Look them up in a dictionary and familiarize yourself with them.

- assumption
- usury
- dispensing

## Requirements of Capacity

*Can you think of some people who might not be able to enter into contracts?*

For a contract to be valid, offer, acceptance, genuine agreement, capacity, legality, and consideration are required. Whenever people negotiate the terms of a contract, they assume that everyone has the power or capacity to do so. **Capacity is the legal ability to enter into a contract.** The **assumption** that another person has the capacity to contract is called rebuttable presumption. The law allows some people to say after the fact that they did not have the capacity to enter into a contract.

### Contractual Capacity Rules and Limitations

According to the law, several types of people may have the right to disaffirm a contract: minors, people with mental impairments, and people under the influence of drugs or alcohol.

**People with Mental Impairments** People with mental impairments can argue that they cannot be bound by contract. A mental impairment could be an injury. It could be a physical problem that someone has had from birth. It could also be a psychological problem that was recently diagnosed. The law only says that if a person had a mental problem when he or she entered a contract, then that person may not be bound to the contract. The mental problem must have made it impossible for the person to understand what was going on when the contract was made. The law requires doctors, not lawyers or judges, to determine if someone is mentally impaired.



#### As You Read

**Predict** Can minors cancel contracts to which they have agreed?



#### Contracts and Minors

Minors have rights and duties when it comes to contracts. They may, for example, change their minds and terminate a contract they have entered. However, they must be truthful about their age when making agreements. *How does this apply to buying movie tickets?*



Sometimes, people have a mental problem that is so severe they cannot take care of themselves. If the court decides that is the case, it will appoint a guardian for that person. The mentally impaired person's contracts are then declared void. This means that the person cannot make any contracts at all.

It is also possible that a contract made by a person with a mental impairment is perfectly valid. If the person was not suffering from the impairment when the contract was made or, if suffering from the impairment, the person still knew what he or she was doing at the time, then the contract is valid.

**Minors** Most of the time, minors are able to enter into and honor contracts. The law allows minors to get out of contracts. It considers them too inexperienced, immature, unknowledgeable, or naive to be permitted to enter into contracts without some sort of protection. If a minor does decide to get out of a contract, most adults choose not to fight it. To make contracts, there are a number of rules that minors must follow. Adults can also protect themselves from deceitful minors by refusing to enter into contracts with minors, unless parents also enter the contract. This approach is generally used for very expensive items such as cars. It protects the adult by obligating the parents if the minor tries to escape the contract.

**A minor is a person who has not yet reached the age of adulthood.** Sometimes we say that a person who is still not an adult is in his or her minority. A person who has reached the age of adulthood is said to have reached his or her majority.



## Case Study – Kiefer v. Fred Howe Motors, Inc.



**Critical Thinking** *Under what circumstances should you be held to a contract you signed when you were a minor?*



Note key facts in the text below and look up words you do not understand. Restate difficult ideas in your own words. Go back and reread the text quickly to make sure you did not miss any important detail. Now, you are ready to formulate an opinion.

**A Minor Problem?** Steven Kiefer was 20 years old and married when he decided to buy a car from Fred Howe Motors, Inc. He signed a contract with the car dealer that included the statement: "I represent that I am 21 years of age or over and recognize that this dealer sells the above vehicle upon this representation."

After Mr. Kiefer turned 21 (the age of majority in the United States at that time), the car started having problems. Mr. Kiefer wanted to return the car to the dealer. He argued that because he was a minor when he signed the contract, the contract was voidable. The car dealer argued that Mr. Kiefer was no longer a minor, and that because he was married when he signed the contract, he was emancipated from his parents.

*Kiefer v. Fred Howe Motors, Inc., 158 N.W.2d 288 (Wis. 1968)*



Go to [glencoe.com](http://glencoe.com) for more case study practice.

**The age of majority is 18 in most states.** Many states have made the drinking age 21, the age at which someone may legally purchase or consume alcohol. In most states, however, the age at which a person can legally purchase tobacco products is 18.

In the eyes of the law, people reach a particular age at the beginning of the day before their birthday. The law does not deal in fractions of days. One second after the clock strikes midnight means that the entire new day has been counted by the law. On your eighteenth birthday, you are legally considered eighteen and one day old.

**An emancipated minor is one who is no longer under the legal control of his or her parents.** Emancipated minors are responsible for their own contracts. Minors are automatically emancipated when they get married or set up their own households. Minors may also seek a court's permission for emancipation by suing for emancipation.

Minors who claim to be adults are committing fraud. In some states, when minors lie about their age and then insist on getting out of a contract, the other parties may sue for fraud. All five elements of fraud (see Chapter 6) must be proven for such a lawsuit to succeed. Other states still follow a much older rule that says minors cannot be sued for fraud, even if they lie about their age. These states still see it as a criminal offense when minors lie about their age to get age-restricted products, such as cigarettes and alcohol.

**Intoxicated Persons** People who are under the influence of drugs or alcohol can sometimes get out of a contract. Persons claiming intoxication must have been so impaired that they did not know what they were doing when they entered the contract. This decision is made by a judge or a jury.

**Other Limits on Capacity** In a few states, convicts have a limited capacity to contract. Aliens, citizens of other countries living in the United States, may also have limited contractual capacity. In wartime, foreign-born people identified as enemy aliens may be denied certain legal capacities.

The law makes exceptions when contracts involve necessities such as food, clothing, shelter, medical care, and other things a person needs to live. It is up to a judge or a jury to decide whether a particular item is necessary.

## Rights and Duties of Minors

Contracts made by minors are voidable by the minor. This means that minors have the right to disaffirm, or avoid their contracts if they choose. **To disaffirm a contract means to show the intent not to live up to the contract.** This intent can be shown by action or by statement. Minors can disaffirm contracts even when they have used poor judgment.

**Returning Goods** Minors who still have the goods they purchased when they disaffirm sales contracts must return those goods within a reasonable time. What reasonable time is, is decided by a judge or jury.

## Reading Check

**Enumerate** What statutes that affect capacity should you be aware of when entering a contract?



**Returning Goods** Special rules apply to minors when returning merchandise they have purchased. Suppose you have bought a video game and used it for a week. *Could you return it?*



The more perishable the goods, the less time will be considered reasonable. The minor can give back the goods by actually handing the goods over to the other party or by making an offer to do so. In some states an amount can be deducted for damaged, dirty, tattered, and torn items that the minor returns. Young people can also disaffirm a contract after becoming an adult. They must do this within a reasonable amount of time. Sometimes, even minors who no longer have the goods can get out of their agreements.

**Disaffirming Contracts** Minors cannot pick and choose the parts of the contract they want to keep and those they want to disaffirm. When two minors make a contract with each other, both of them can get out of the contract. Minors are, therefore, at risk when they enter a contract with another minor.

If an adult discovers that the other party is a minor, the adult has no right to get out of the contract for that reason alone. Sometimes, people buy goods from somebody who bought the goods from a minor. If the minor then decides to get out of the original contract, the ownership rights of the innocent third party are protected. This rule applies only to goods, not to land.

**Ratification of a Minor's Contracts** **Ratification** is the act of agreeing to go along with a contract that could have been avoided. A person can ratify a contract by words or actions. The words can be spoken or written. A minor can ratify a contract after becoming an adult. Once this is done, all the contractual privileges that the person had as a minor are gone. If a minor makes a payment that is due under a contract after becoming an adult, that minor has ratified the contract.

### Exceptions to the General Rule

The law may use exceptions to the rule that lets minors get out of their contracts. For example, minors must pay the fair value of the necessities. Some states will hold minors to contracts for things required by law, such as car insurance. Some states give limited capacity to minors who own businesses. Other states say that married minors are adults. Others treat an apartment rental agreement as a contract for a necessary. Minors also cannot get out of military enlistment agreements.

**Minors as Drivers** Driving is a privilege, not a right. As a privilege, it must be earned, and then kept under conditions of good behavior. Many states will not permit minors to earn a license until they reach the age of 16.

Minors must also meet certain minimum requirements before earning a license. The requirements generally include a written test to qualify for a temporary driving permit, a driver's education course, and a final examination that consists of a road test and a vision exam. A minor with a driver's license generally has the same rights and responsibilities as an adult driver.

**Minors as Students** Students in a school setting may be searched if school officials have reason to suspect the law or a school rule has been broken. While adult speakers and writers are granted freedom in how they can express themselves in speech or in print, students may be restrained from printing certain matters in a school-sponsored newspaper.

## The Rights and Duties of Parents and Guardians

Parents have certain rights under the law. They have the right to discipline their children and to manage their children's property. Adoptive parents have the same rights. Neither natural nor adoptive parents can abuse those rights.

The law protects children from abusive parents under the *parens patriae* doctrine. This doctrine holds that the state can act as a child's parent when natural or adoptive parents cannot or will not perform their parental duties.

The law also states that both natural and adoptive parents have the duty to provide their children with necessities. If minors are forced to purchase the necessities on their own, the parents will be liable for that contract. If a minor becomes emancipated, parental duties come to an end.

In their wills, parents may name guardians for their minor children. Two types of guardians can be appointed by the parents. Guardians of the child will act as the parents would act in relation to the child. Property guardians will handle the child's property. This right ends when the child reaches the age of majority.

## Legality

*Is a contract valid if one of its terms breaks the law?*

Illegality can destroy an otherwise valid contract. It can also expose people who agree to the contract to potential charges of criminal conduct and other legal consequences. While most laws are widely known and understood, there are many laws against doing things that are not so obvious, such as having a yard sale without a license. These laws create what is called a hidden dimension of illegality.

## Effect of Illegality

In general, a court will not help any party to an illegal contract. Instead, it will leave the parties where they put themselves. Neither party can enforce the agreement. Neither party can get help from the court. An exception is made when the parties are not equally at fault. In such cases, the court may help people who are less at fault in getting back any money or property they may have lost.



**Illegal:** *adj* Against the law. From Latin *il* = not + *leg*, *lex* = law: not lawful.

*In pari delicto:* Latin adverbial phrase = in equal fault.

**Vocabulary Builder** *Il*, *im*, *in*, or *ir* at the beginning of a word (that is, as a prefix) often means not. List five words that begin with these prefixes and define them using the word not. For example, improper = not proper.

**Look It Up!** Check definitions in *Black's Law Dictionary* or an online glossary. For direct links, go to [glencoe.com](http://glencoe.com) to find more vocabulary resources.

**Illegality in Entire Agreement** Sometimes, a contract cannot be divided into separate promises and different acts. If a contract cannot be divided, then anything illegal within the contract makes the entire contract illegal. The whole contract is, therefore, void. This is true even if sections of the agreement are legal.

***In Pari Delicto* and Divisible Contracts** If certain promises and actions in a contract can be performed by themselves, the contract is divisible. The courts may enforce parts of the agreement that are legal and cancel the parts that are not.

The parties are said to be in *in pari delicto* (in equal fault) if they both know that the agreement is illegal. In that case, the court will not help either party. On the other hand, if one party is not aware of the illegality and had no intent to break the law, then the parties are not in *in pari delicto*. The courts may grant relief to the innocent party.

## Agreements That Break Statutes

State legislatures pass laws that make some agreements illegal because they violate the state's civil or criminal statutes, **usury** statutes, gambling statutes, licensing statutes, or Sunday statutes.

**Civil and Criminal Statutes** Agreements that require one party to commit a tort or a crime are illegal. Common torts are slander, libel, and fraud. Crimes include burglary, larceny, murder, and arson. An agreement is illegal if it is made to interfere with or to violate the rights of another person. Agreements to protect one party from the consequences of the torts or the crimes he or she has committed are also illegal.

**Usury Statutes** A contract to buy stolen goods or commit arson is obviously illegal. Usury, however, is an example of an activity that has the hidden dimension of illegality. Interest is the fee a borrower pays to a lender for using money. Usury is charging more than the maximum legal interest rate. Each state has a statute that sets a maximum interest rate that lenders can charge for loans. Charging whatever you want for interest is not only unfair, it is also illegal.

The Truth in Lending Act is one step the federal government has taken to make consumers aware of the cost of borrowing money. Under this law, the lender must clearly report the annual percentage rate (APR) to the borrower. Before you sign any loan agreement or credit card, look for the true rate of interest (APR).

**Gambling Statutes** Gambling statutes fall within the hidden dimension of illegality: Playing cards, betting on sports events, or entering an office pool for money may seem harmless, but they are illegal in many states. If you win money gambling but have trouble collecting, the court will not enforce the debt, and may consider you to be in violation of the law.


Today, many types of regulated gambling are legal. A state may legalize one form of gambling and outlaw others. One form of gambling might be legal in one state but not in another.

Giveaway games by stores or businesses for promotion are legal as long as you are not required to buy a ticket or product to participate. Betting at racetracks is allowed in New York, Illinois, California, Massachusetts, Ohio, and some other states. Lotteries, other than those run by the state government, are still illegal in many places. Many states have set up their own state-run lotteries to raise money.

**Sunday Statutes** In early colonial days, some American colonies passed special Sunday statutes, also called blue laws, that made agreements made on a Sunday void. An offer made on a day other than Sunday, but accepted on a Sunday, is void. If an offer is made on a Sunday but accepted on another day, the contract is valid because acceptance marks the creation of the contract. If an agreement is made on a Sunday, but a date other than Sunday is placed on the agreement, the contract is void. States that still observe Sunday laws often apply the same restrictions to legal holidays.

**Licensing Statutes** All states have statutes that require a license to do certain jobs. A license is a legal document that grants permission from the government to do a certain job. Licenses protect people from dealing with unqualified persons. Trade and professional people such as nurses, doctors, lawyers, funeral directors, barbers, and plumbers must be licensed. An agreement made with an unlicensed person working in such jobs is illegal. Some state statutes require licenses simply to raise money. Any person who pays the fee gets a license. A law requiring a vendor's (seller's) license is designed to raise revenue for the local government that issues the license. In these cases, agreements made with unlicensed people are valid. However, the unlicensed person might be fined.



 **Special Statutes** Doctors and most people in medical professions have to obtain and display a license to practice medicine. *What is the purpose of licensing medical personnel?*




## Agreements Contrary to Public Policy

Not all illegal agreements break statutes. Some agreements are illegal because they break public policy. The power to regulate the public's health, safety, welfare, and morals belongs to the government. The states have this power because they have governmental authority. The federal government has this power because of the U.S. Constitution. **Public policy is a legal principle that holds that nobody should be allowed to do something that harms the public.** Public policy allows the courts to get involved to protect the public welfare when other laws do not.

**Agreements That Unreasonably Restrain Trade** The law protects the right to make a living. If a contract takes away this right, the law will label the contract void. Restraint of trade agreements take away somebody's ability to do business with others. Three types of contracts circumvent this rule: agreements not to compete, agreements to fix prices, and agreements to defeat competitive bidding.

**Agreements Not to Compete** When someone buys a business, that person also buys the seller's goodwill not to compete. One way to ensure goodwill is to add a restrictive covenant to a sales contract. A restrictive covenant not to compete is an agreement in which the seller promises not to open a business that competes with the buyer within a certain area for a period of time.

 **Bidding for Public Works Contracts** It is illegal for contractors to engage in any type of price fixing when bidding for public works contracts. *Why does this rule protect the public?*



A court will uphold this agreement, which keeps it out of the hidden dimension of illegality if it is reasonable in time, location, and type of business. If the restraint is unreasonable considering the nature of the business sold, then the restraint is illegal. Promises not to compete are also found in employment contracts. Employees agree not to work at similar jobs for a period of time after they leave this employment. Such contracts are enforced only as needed to protect the former employer.

**Agreements for Price Fixing** In the United States, some laws have been created to protect competition. Price fixing is when competitors agree to set prices within certain ranges. In some cases, competitors agree to sell a particular product or service at an agreed price. In other cases, manufacturers dictate the price at which retailers must sell a product. Price fixing hurts competition and keeps prices artificially high. Because they are contrary to public policy, the courts will not uphold price-fixing agreements. In fact, competitors who seek to fix prices may be prosecuted by state or federal agencies.

**Agreements to Defeat Competitive Bidding** A bid is an offer to buy or sell goods or services at a stated price. Laws often require governments to construct public works or buy goods and services through competitive bidding. In this process, competitors submit bids for a project, and the the lowest qualified bid wins the contract. If competitors agree not to bid lower than a certain price, then they are not bidding competitively. The agreements and the contracts are not enforceable.

**Agreements to Obstruct Justice** A contract that gets in the way of the **dispensing** of justice is illegal. Such contracts include protecting someone from arrest, encouraging lawsuits, giving false testimony, or bribing a juror. It also includes an agreement to pay a non-expert to testify at a trial. It could also include an agreement to take money to stop a legal action against a person who has committed a crime.

**Agreements Inducing Breach of Duty or Fraud** Many persons hold positions of trust and have a responsibility for the well-being of others. Your representative in Congress, your state senator, and all other public officials hold positions of trust. They owe a duty to work for the best interest of the public. Any contract that tries to influence these people for private gain is unenforceable. This rule also applies to private persons who are in positions of trust.

**Agreements to Give Up the Right to Litigate or Arbitrate** Contracts may include clauses that limit the ability of the parties to bring a lawsuit or to arbitrate a claim. Sometimes, such clauses are valid. However, they might be offered on a take-it-or-leave-it basis by the party with the most power. The clause must be fair. If it is not, the court might say it is unconscionable and strike it down as illegal.

**Agreements Interfering with Marriage** Contracts that discourage, damage, or destroy good family relationships are illegal. For instance, if Mr. Popson promises to give his daughter, Angela, \$100,000 if she never gets married, the contract is void.

## The Statute of Frauds

*What happens if you want to make changes to a contract after you agreed to its terms?*

In the past, under common law rule, a person accused of breaking a contract could not testify about it in court. Instead, only people who were not parties to the contract could testify. This encouraged bribery. To prevent this, the English Parliament passed a law in 1677 that required certain contracts to be in writing in order to be enforceable. The law was called An Act for the Prevention of Frauds and Perjuries.



## Global Law

### Contract Differences in Canada

The United States and Canada have a legal tradition based upon English common law. Many of their legal principles, including those dealing with contracts, are similar. Some differences have occurred since the two countries gained their independence from England. Two major differences relate to entering into noncommercial oral contracts and the elements of proving fraud in a contract dispute.

#### Oral Contracts

In the United States, oral contracts are considered as valid as written contracts for almost everything except the sale of real estate.

In Canada, however, there is a presumption that people do not enter into oral contracts for non-business, religious, or charitable reasons. This includes entering into contracts with family members and friends.

This is demonstrated in a case in which a Canadian court held that an agreement entered

into by friends to share a set of season hockey tickets was not a valid oral contract because it was not for business reasons.

#### Fraud

Another contract law difference between the United States and Canada relates to fraud. In the United States, the parties must prove that the victim suffered an actual loss from the fraud in order to recover losses. In Canada, a loss is not required to recover damages against the perpetrator of the fraud. This can be especially advantageous when the victim wishes to rescind or cancel a contract before harm occurs.

#### Across Cultures: Quebec's Legal System

Most Canadian provinces have a common law system. However, Quebec has a civil code system inherited from the French; so does the state of Louisiana in the United States.

**Critical Thinking** *Would an oral agreement between neighbors for splitting the cost of a fence be considered a valid oral contract in Canada? In the United States?*

Today, most states in the United States have a Statute of Frauds. A **Statute of Frauds is a state law that requires that certain contracts be in writing.** This is so there is evidence that (1) the contract exists, and that (2) it has certain definitive terms.

## Elements of a Written Contract

A written contract can be a letter, a sales slip, an invoice, or several words placed on a check. There are some specific requirements. The written contract must, for example, identify the place, date, parties, subject matter, price and terms, and intent of the parties. It should also contain the signature of the party who may be charged.

**Interpretation of Contracts and Clashing Terms** It may be necessary to make changes to a contract in handwriting because it is too inconvenient to print a whole new contract. The court will enforce handwritten terms. The court assumes that the handwritten changes were placed in writing after the contract was printed and represent the final intent of the parties. According to the law: (1) handwriting prevails over typewriting, preprinting, or word processing; (2) typewriting or word processing prevails over preprinting. The court will honor the amount on a check that is written in words.

When a written contract is filled with confusing language, the court will lean against the party who actually wrote the contract. Words, phrases, and sentences should be clear and unambiguous.

## Contracts That Must Be in Writing

The Statute of Frauds adds a requirement to the six elements of a valid contract: offer, acceptance, genuine agreement, capacity, consideration, and legality. Certain contracts must be in writing to be enforceable. Be aware that the Statute of Frauds applies only to executory contracts (contracts that have not been fully performed).


**Contracts to Pay Somebody Else's Debt** A contract to pay someone else's debts must be in writing to be enforceable. The debtor still owes the money; the person promising to cover the debt does so only if the debtor fails to pay.

## Contracts to Pay Debts of a Person Who Has Died

When a person dies, somebody has to pay that person's debts and divide up the rest of his or her property among any remaining relatives. Executors and administrators handle such matters. The law says that executors and administrators are not personally responsible for the debts.

Often, executors are close relatives of the deceased. They may feel responsible for the deceased's debts when the estate runs out of money and agree to pay them. Later, the executor might have second thoughts about having made such a promise. To protect someone in such a vulnerable position, the law requires that such an agreement be in writing.



 **Real Estate Contracts** Contracts that involve real estate sales must be in writing. *What is the exception to this rule?*

### **Contracts Requiring More Than a Year to Perform**

Any contract that cannot be performed within one year must be in writing to be enforceable. The year begins to run when the contract is made, not when the performance is to start. Agreements in which the amount of time involved is uncertain do not have to be in writing.

**Contracts in Consideration of Marriage** When two persons agree to marry, they enter into a contract. The promises they make to each other are consideration for the contract. Agreements to marry have never required a written contract. Under present-day law, an agreement between two people to marry is not enforceable. Either party can break the agreement. If one person agrees to marry another person for a third person's promise of money or property, the agreement must be in writing. A promise to adopt a child from a former marriage or to care for another relative in return for a promise of marriage must be in writing to be enforceable.

**Contracts for the Sale of Goods** Although the Uniform Commercial Code (UCC) lists many exceptions to this rule, a contract for the sale of goods for \$500 or more must be in writing.

Goods are movable items such as furniture, books, computers, PDAs, cultivated crops, clothing, vehicles, and MP3 players.

According to the UCC, a written agreement is valid if it indicates that a contract for sale has been made between the parties. The UCC does not require that all the terms of the contract be in writing.

**Contracts to Sell Real Property** Contracts for the sale of real property must be in writing to be enforceable. Real property is land and anything permanently attached to the land. One important contract for real property you might enter into is the contract to buy or sell a home. The contract of sale, sometimes called a purchase and sale agreement, consists of an offer that is made by the buyer and accepted by the seller.

One major exception to the requirement that a contract for the sale of real property be in writing is called equitable estoppel. According to equitable estoppel, a party cannot claim the Statute of Frauds if the other party did something extreme, such as making excess improvements to the property, because of what the other party promised.

## Special Rules for the Interpretation of Contracts

It is crucial to understand which contracts must be in writing to be enforceable in a court of law. There are also special rules for the interpretation of written contracts. These rules include the parol evidence rule and the best evidence rule.

**The Parol Evidence Rule** A written contract should contain everything that was agreed upon between the parties so that neither party can go to court and claim a contract is incorrect or fails to show the parties' real intentions.

This long-established rule is called the parol evidence rule. Parol means word of mouth; evidence, in this instance, means anything presented as proof in a trial. The parol evidence rule says that evidence of oral statements made before signing a written agreement cannot be presented in court to change or add to the terms of that written agreement. The court presumes that a written contract contains all of the terms and provisions intended by the parties.

There are exceptions to this general rule. Parol evidence may be introduced to explain some point that is not clear in a written agreement. It may be used to show that certain terms were incorrectly placed in the written contract. It also may be presented to prove that one party was tricked by another.

**The Best Evidence Rule** This rule requires that the original written agreement (rather than a copy) be used as evidence in court. The rule means a court does not want to look at photocopies or faxed copies of a written agreement. Copying a contract can make it easier for a dishonest person to hide alterations to the original. For this reason, when a contract is reduced to writing, each party receives an original version of the contract.

Duplicate originals are original versions of a contract that are signed by and provided to all of the parties to a contract.

**Real-World Rules** When you are asked to sign an order blank, sales slip, or other printed form, such documents may contain small print on the front or reverse side. The words are often difficult to read, and the language may be hard to understand. Often, the small print is not written in your favor. Follow these guidelines before you sign:

- Read the entire text of the document before you sign it.
- If you do not understand something or do not agree to it, cross it out before you sign. Do not be shy about having the other party initial the change too. The change is meaningless unless the other party has initialed it.
- Do not be afraid to make changes on a printed or word-processed form. If any extra-added promises are made to you, write them in.
- If a contract is for something major, such as the purchase of a house or car, and contains a lot of legal language—or legalese—you do not understand, have a lawyer review it before you sign.
- Refuse to sign a written contract if you do not agree with everything contained in the writing.

### After You Read

**Summarize** What should you consider when you are evaluating a contract?



## SECTION 5.1 ASSESSMENT

### Self Check

1. What rights does a minor have in relation to contracts?
2. What happens when a minor becomes emancipated?
3. How are minors protected under the *parens patriae* doctrine?

### Academic Connection

**Mathematics** As a part of your sales contract with Wilson Sporting Goods Company, you are entitled to a trade discount. The invoice is for \$1,454.00

with the terms 6/15/n30, which means that if your bill is paid within 15 days of receipt you receive a 6% discount. If you take the full 30 days to pay, no discount applies. Calculate the discount and the amount due for the invoice.

**THEORY** **Number and Operations: Use Fractions, Decimals, and Rounding** To solve this problem use the following formulas:

$$\text{Cash Discount} = \frac{\text{Net Price}}{\text{Price}} \times \frac{\text{Cash-Discount Rate}}{\text{Rate}}$$

$$\text{Cash Price} = \frac{\text{Net Price}}{\text{Price}} - \frac{\text{Cash Discount}}{\text{Discount}}$$



For more math practice, go to the Math Appendix.

### Critical Thinking

**Contracts between Minors** Suppose that you have purchased an MP3 player from a classmate. Can that classmate change his mind, ask you to return the player, and offer you a refund? Explain.



Go to [glencoe.com](http://glencoe.com) to check your answers.

# Consideration

## SECTION 5.2

### Reading Guide



#### Before You Read

**Connect** If you agree to sell your MP3 player to your best friend for \$50, what do you gain and what do you lose? What does your friend gain and lose?

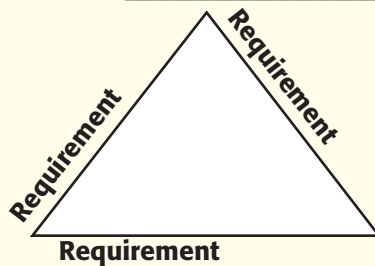
#### Focus on Ideas

Consideration is a kind of exchange and it is a key element of a valid contract.

#### Take Notes

Create a graph like the one shown and use it to take notes as you read this section. Go to [glencoe.com](http://glencoe.com) to find graphic organizers and tips on how to improve your note-taking skills.

**Consideration  
Definition:** \_\_\_\_\_



#### Key Terms

You will learn these legal words and expressions in this chapter. You can also find these terms in *Black's Law Dictionary* or in an online legal dictionary.

- consideration
- forbearance
- unconscionable contract
- adhesion contract
- accord and satisfaction
- promissory estoppel



#### Academic Vocabulary

You will find these words in your readings and in your tests. Look them up in a dictionary and familiarize yourself with them.

- contain
- indicating
- obligation

### What You'll Learn

- ◆ Analyze the requirements for valid consideration.
- ◆ Define the different types of consideration.
- ◆ List exceptions to the requirements of consideration.
- ◆ Compare unconscionability and illegality.

### Why It's Important

Understanding the concept of consideration will help you make sure that contracts you enter into are valid.

### Academic Standards

Reading and completing the activities in this section will help you practice the following academic standards:

**English Language Arts (NCTE 3)** Apply a wide range of strategies to comprehend, interpret, evaluate, and appreciate texts.

**Math (NCTM PSS 2)** Solve problems that arise in mathematics and in other contexts.



## As You Read

**Predict** Does a contract have to include an exchange to be valid?



**Vocabulary** You can find vocabulary definitions in the **Key Terms** glossary and **Academic Vocabulary** glossary in the back of this book.

# The Legal Concept of Consideration

*Is ordering a taco at a street stand consideration?*

**Consideration** is the exchange of benefits and detriments by the parties to a contract. A benefit is something that a party receives in the agreement. A detriment is something a party gives up in the agreement (see **Figure 5.1**). There are three types of detriments:

- Giving up something that you have the right to keep
- Doing something that you have the right not to do
- Not doing something that you have the legal right to do

The last type of detriment listed is also called forbearance.

**Forbearance** is not doing what you have the right to do.

## Requirements for Valid Consideration

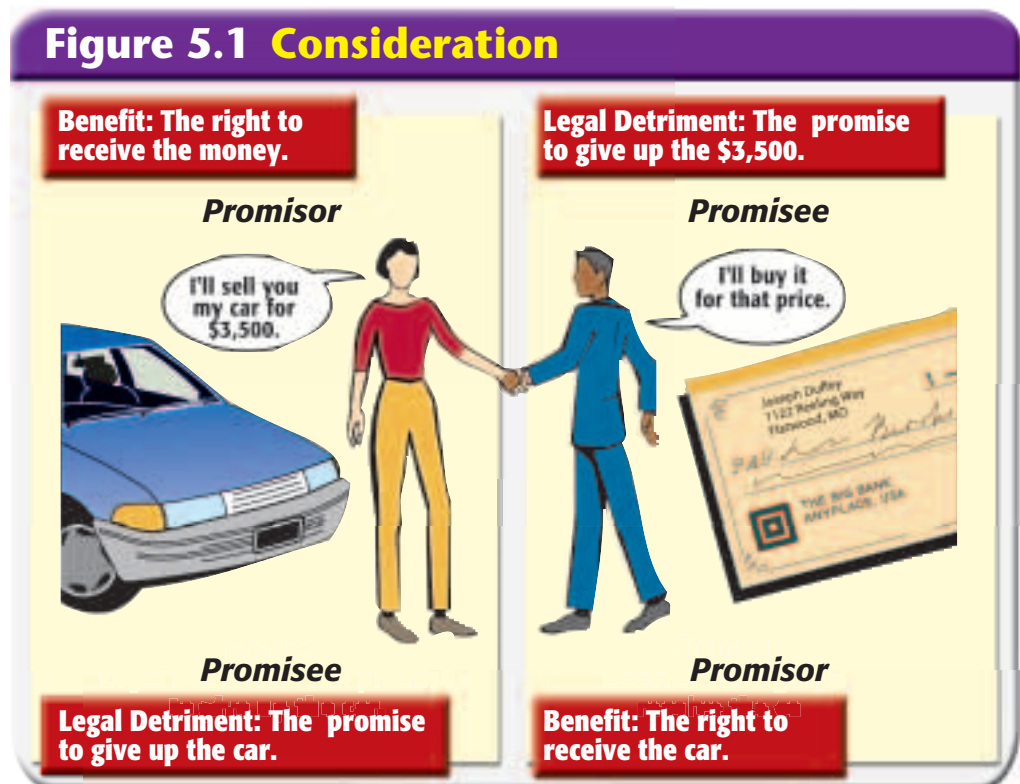
The parties must bargain with each other if there is to be a contract. Each side in the agreement must give up something and get something in exchange. The exchange or the promise to exchange something of value is what binds the parties together. A date for Friday night or a promise to pick up a friend before school are not contracts because neither one **contains** consideration.

## The Characteristics of Consideration

There are three characteristics of consideration:

- Consideration must involve a bargained-for exchange.
- Consideration must involve something of value.
- The benefits and detriments that make up consideration must be legal.

**Figure 5.1 Consideration**



**Consideration** Consideration is an exchange of benefits and detriments by the parties to an agreement. *Is consideration necessary to make a contract legally binding?*



## Business ETHICS

### Cheap Computers

Suppose you work for a computer manufacturer. You have two outdated personal computers at home you want to replace. You work out an arrangement with a fellow employee, who is a salesperson for the company, to get a great deal on two new computers. A contract is drawn up where you will buy the computers from the company for \$5 each, even though each computer retails for \$1,500.

**Critical Thinking:** *Is there consideration in the contract? Should you sign the contract?*

**Bargained-for Exchange** A contract involves a bargained-for exchange when a promise is made in return for another promise. It also occurs when an act is exchanged for an act or a promise not to act. Bargaining means that a party will lose something if the other party does not come through as promised. Conversely, both parties gain something when the promises are kept or the acts are performed.

**Something of Value** Something of value to one person may be worthless to another. The law is not concerned with the value of consideration and does not set value in a contract. All that matters is that the parties agree freely on the value and the price, and that consideration be present and the parties agree to it.

The only time a court might look at the value of consideration is if it thinks that the consideration offered is so far from what it should be that it is grossly unfair. This type of contract is said to be unconscionable. **An unconscionable contract is an agreement in which the consideration is so out of line with the actual value of the subject matter and so unfair that it shocks the court's conscience.**

Two additional conditions must be present for a contract to be unconscionable:

- There must be uneven power between the parties.
- The party with all the power tells the other party to take it or leave it.

This is called an adhesion contract. **An adhesion contract is a take-it-or-leave-it offer made by a party who holds most of the power in a bargaining session.** When the courts are faced with this type of situation, they will do one of three things:

- Refuse to enforce the entire contract.
- Enforce the contract without the unconscionable clause (if possible).
- Limit the enforcement of that clause.



### Reading Check

**Enumerate** List three common types of consideration.

**Legality and Unconscionability** The law requires that the consideration that passes from one party to another be legal. If the consideration is illegal, the contract is void. For example, someone cannot give up something, such as a stolen bicycle, that he or she does not own. Illegality is not the same as unconscionability. Consideration may be legal, as when money is paid for an item, but unconscionable because the amount paid is so unfair that it shocks the conscience of the court.

## Types of Consideration

*If you agree to sell your laptop to a classmate, what do you think consideration could be?*

There are very few limits on what consideration can be: it is what two parties agree it should be. Courts see some everyday things as consideration: money, property, services, promises not to sue, and promises made to a charity (see **Figure 5.2**).

### Money as Consideration

Often, one party offers money in exchange for the other party's property or services. Sometimes, when costs get out of hand, the government might step in and control prices. There are also a few laws, like the Federal Fair Labor Standards Act, which sets a minimum wage for workers, that dictates the amount that can be offered in certain contracts.

### Property and Services as Consideration

Service as consideration is part of a contract with some workers; for example, when your family hires a gardener to take care of the lawn or a plumber to fix a leaky pipe or when you buy the services of the hair stylist who cuts your hair. Property is also consideration. This is the type of agreement you enter whenever you go to the mall to buy CDs. Contracts for the purchase of a new house are another example. Property is consideration in barter agreements, such as when you trade video games with your friends.

### A Promise Not to Sue

Giving up the right to sue is a type of forbearance. Lawsuits are often settled when one party agrees not to sue the other party. The other party promises to pay a set amount of money in return. A signed agreement not to sue is called a release. This practice is so common that many insurance companies have preprinted forms that they use to settle cases before they even get filed.

### Charitable Pledges

Charities depend on money from businesses and individuals. This has led the courts to uphold donation promises as if they were contracts, although there often is no consideration in the agreement. Courts uphold these pledges because charities provide services to society.

## Figure 5.2 Types of Consideration

**Service** as consideration involves exchanging work or expertise for goods or money, such as when you contract someone to repair your computer or cut your hair.




**Property** as consideration involves the exchange of goods for money, services, or other goods. Exchanging goods for other goods, such as trading video games or CDs with a friend, is called barter.



**Money** as consideration, which can be in the form of credit or a paycheck, involves the exchange of money for goods or services.



 Money, property, and services are the most common forms of consideration in a contract. *What are two other forms of consideration?*


## Problems with Consideration

Sometimes, the parties to a contract disagree on how much money is due. There is a way out of such disagreements. The solution depends on whether there really is a genuine disagreement as to the amount that is owed.

**Disputed Amounts** If there is a genuine issue as to the amount owed, the parties can use accord and satisfaction to settle the argument.

**Accord and satisfaction is a legal way to settle contractual disputes by which one party agrees to accept less than the amount due as full payment.** The acceptance by the creditor of less than what was billed is the accord. The agreed-to settlement as contained in the accord is the satisfaction. The dispute must be real and in good faith. Finally, the amount involved cannot be trivial.

**Example:** Alison and Jeremy Brisbane made a contract with the Port Clinton Construction Company to put siding on their house in Lakeside, Ohio. The company charged \$50 per hour for a job that lasted 200 hours. The final bill for labor was \$11,250. When they looked at the bill, the Brisbanes saw that they had been charged an hour per day for travel time from the company's home base to their house. The Brisbanes thought it unfair for them to be charged for travel time. They deducted \$1,250 from the bill (25 travel hours at \$50 per hour). They sent a check for \$10,000 to the company. On the check, they wrote, "In full payment for the siding placed on our summer home at 206 Jasmine, Lakeside, Ohio." When Port Clinton Construction cashed the check, they accepted the lesser amount as full payment.

 **Amount Due Disagreement** A contractor and a homeowner might not agree on an amount due in exchange for work performed. *In what case could accord and satisfaction not be used to settle the issue?*



**Undisputed Amounts** If the parties have agreed to a set amount of money in the contract, then accord and satisfaction does not apply. This is true even if the party who owes the money finds out that the product was on sale for a lesser amount somewhere else.

## Exceptions to the Requirements of Consideration

Some agreements are valid even without consideration. Specific rules vary from state to state, but some agreements always fall into this group.

**Promises Under Seal** A seal is a mark or an impression placed on a written contract **indicating** that it is a formal agreement. Most states today do not require a seal. Those that do generally allow the word seal on the letters, L.S., or the phrase *locus sigilli* (place of the seal) after the signature. Contracts for goods do not require a seal. Some contracts for land do need a seal.

**Promises After Discharge in Bankruptcy** Sometimes, people who have had their debts discharged in bankruptcy court promise to pay the debts anyway. A court hearing is required when such promises are made. In the hearing, the debtor is told about the legal consequences of making such a promise. Some states do not require any consideration for this promise. The promise is supported by contractual intent. Some states say the promise must be in writing.

**Debts Ended by the Statute of Limitations** A statute of limitations sets up the time limit for suing somebody. Different states have different time limits. Such variations can run from three to ten years. The same state may also have different time limits for different types of contracts. For instance, the statute of limitations may set one time limit for oral contracts and a different one for written contracts. A time limit for a contract for goods may be different from a contract for the sale of real property.

**Promises Enforced by Promissory Estoppel** If someone making a promise should have reasonably expected the other person to rely on the promise, and the other person did rely on the promise and suffered a loss, the innocent party can use promissory estoppel to make the other party compensate him or her for the loss. The doctrine stops one party (the estoppel part) from denying that he or she made a promise that hurt the second party (the promissory part). **Promissory estoppel is the principle that a promise made without consideration may nonetheless be enforced to prevent injustice.** The following elements must be present:

- The promise was made about the innocent party's action (or lack of action).
- The innocent party gave no consideration in exchange for that promise.



### **Preexisting Duty**

Preexisting duties cannot be made consideration in a new contract. *Why does the law prevent preexisting duties from being consideration in new contracts?*

- The innocent party relied on the promise and did something that changed his or her position in a major way (such as sold a car, moved out of an apartment, sold a house, or took a vacation).
- Injustice can be avoided only by enforcing the promise and making up for the loss.

**Option** Sometimes one person will pay another person money to keep an offer open for a set period of time. This is called an option. When the contract involves goods, the offer can be held open without the money payment. This is called a firm offer. A firm offer requires a written offer stating the period of time during which the offer will stay open. The time cannot go beyond three months. The person making the written offer must be a merchant who deals in the types of goods involved on an everyday basis.

### **Agreements without Consideration**

Some agreements and promises seem to include consideration, but in reality they do not, and what passes for consideration is actually not enforceable by law.

**Illusory Promises** For a contract to be real, all the parties must be required to do something. Sometimes, a contract seems to require something when it really does not. For example, this happens when a restaurant agrees to buy all the apples it needs for the summer from a particular farmer. The promise seems real, but since the restaurant can simply say it did not need any apples that summer, the promise is not real. This is an illusory promise.

**Future Gifts and Legacies** A person's promise to give a gift to another person at some time in the future or to leave a legacy in a will cannot be enforced without consideration. This rule applies to promises of free services or to promise to lend somebody something.

**Past Consideration** The act of giving consideration must happen at the same time that the contract is made. Past consideration is something that was given or promised in the past that somebody tries to use again in a new contract. The courts do not accept past consideration. For example, suppose you help your older brother move into his college dormitory on Saturday. The next day, he promises to pay you \$25 for helping. That promise is not binding because your consideration was given in the past.

**Preexisting Duties** The act of giving consideration requires a new promise for every new contract. A preexisting duty is an **obligation** that a person already has to do something and cannot be used again in a new contract. Suppose a person is already obligated to do something, such as mow the lawn every week. Then he or she cannot make it consideration in a new contract. If the courts allowed preexisting duties to bind a party in a new contract, they would be permitting one promise to do double duty.

**Promise to Attend a Social Engagement** All contracts are agreements, but not all agreements are contracts. A promise to take a friend to a concert would not be a legally binding agreement because the friend has given nothing in exchange for the promise: That agreement lacks consideration.



### After You Read

**Summarize** What are contractual situations in which consideration does not apply?

## SECTION 5.2 ASSESSMENT

### Self Check

1. What are the characteristics of consideration?
2. What is an unconscionable contract?
3. What is forbearance?

### Academic Connection

**Mathematics** Mikiko Iwayama purchased a vacuum cleaner for \$299.99. She lives in Wisconsin where the sales tax is 5%. What is the total amount that she will pay for the appliance? Does this purchase constitute a

contract? What is consideration in this case?

**CONCEPT** **Number and Operations: Computing Percentages** To solve this problem use the following formulas:

$$\text{Sales Tax} = \text{Selling Price} \times \text{Sales Tax Rate}$$

$$\text{Total Purchase Price} = \text{Selling Price} + \text{Sales Tax}$$



For more math practice, go to the Math Appendix.

### Critical Thinking

#### Accord and Satisfaction

Suppose that you make a contract to buy a skateboard for your friend, Hal. You then see the exact same skateboard on auction on eBay. You monitor the auction and discover that the winning bidder paid a lot less than you paid Hal. Can you use accord and satisfaction to pay the lesser amount for the skateboard? Explain.

Go to [glencoe.com](http://glencoe.com) to check your answers.



# Chapter 5 Review and Assessment

## Summary

### Section 5.1 Capacity and Legality

- ◆ Capacity is the legal ability to enter a contract.
- ◆ People who lack contractual capacity are: minors, people with mental impairment, and intoxicated persons.
- ◆ The law makes an exception when the contract involves necessities. Necessaries are food, clothing, shelter, and medical care.
- ◆ Minors who decide to get out of their contracts can do so. A minor is a person who has not yet reached the age of adulthood.
- ◆ An emancipated minor is no longer under the control of his or her parents. Emancipated minors are responsible for their own contracts.
- ◆ Minors who claim to be adults are committing fraud.
- ◆ Minors must disaffirm an entire contract. They cannot pick and choose the parts of the contract they want to keep and those they want to disaffirm.
- ◆ Ratification is the act of agreeing to go along with a contract that could have been avoided.

### Section 5.2 Consideration

- ◆ Consideration is the exchange of benefits and detriments by the parties to a contract. A benefit is something received in the agreement. A detriment is a loss.
- ◆ Consideration must involve a bargained-for exchange. It must involve something of value.
- ◆ Consideration includes money, property, and services. Other forms of consideration include promises not to sue and promises made to a charity.
- ◆ Accord and satisfaction is a legal way to settle contractual disputes by which one party agrees to accept less than the amount due as full payment.
- ◆ Agreements valid without consideration: promises under seal, promises after discharge in bankruptcy, debts ended by statute of limitations, promises enforced by promissory estoppel, and options.
- ◆ Agreements not valid without consideration: illusory promises, promise of future gifts or legacies, promises based on past consideration or on preexisting duties, and agreements to attend social engagements.

## Vocabulary Builder

1 On a sheet of paper, use each of these terms in a sentence.

### Key Terms

- capacity
- minor
- majority
- emancipated
- disaffirm
- ratification
- public policy
- Statute of Frauds
- consideration
- forbearance
- unconscionable contract
- adhesion contract
- accord and satisfaction
- promissory estoppel

### Academic Vocabulary

- assumption
- usury
- dispensing
- contain
- indicating
- obligation



Go to [glencoe.com](http://glencoe.com) to play a game and improve your legal vocabulary.

**Key Points Review**

Answer the following questions. Refer to the chapter for additional reinforcement.

- 2 Who determines whether a mental impairment compromised a person's ability to enter a contract?
- 3 What is the rule that determines if someone is so intoxicated that he or she cannot be held responsible for any contracts entered while in that state?
- 4 Can minors disaffirm part of a contract?
- 5 How can adults protect themselves from deceitful minors?
- 6 Why do the courts refuse to become involved trying to set the value of consideration?
- 7 Is it okay to agree to do something that might be considered illegal as consideration in a contract? Explain.
- 8 What ordinary things might be consideration in a contract?

**Standardized Test Practice**

- 9 Read the following information about the Census Bureau and complete questions 1 and 2.

The Census Bureau conducts many censuses and surveys. The most well known is the official population census of the United States, called the decennial census. It is conducted every ten years, most recently in April 2000. During each decennial census, the Census Bureau collects data from every household in the U.S. and its territories.

Besides the decennial census, the Census Bureau conducts nearly one hundred other surveys and censuses every year. By law, no one is permitted to reveal information from these censuses and surveys that could identify any person, household, or business. Individual records from each decennial census are made public 72 years after the census has been taken.

**1. How often does the Census Bureau conduct the decennial census?**

- A every eight years
- B every five years
- C every six years
- D every ten years

**2. By law, what information cannot be revealed?**

- A identify any person, business, or income records
- B identify any person, household, or business
- C identify any person, household, or individual record
- D identify any person, census taker, or business

**Test-Taking Strategies**

Read the stem of the question carefully, then read each of the possible answers all the way through.



## Apply and Debate

Read the following scenarios. Get together with other students in pairs or groups of three and take a position on each scenario. Debate your position in class with students taking the opposite position or prepare a written argument justifying your position.

### 10 Emancipation

Kirsten is 17 and a senior in high school. For the past six months, she has not been getting along with her parents and wants to move out on her own. Her parents reject this idea, so Kirsten decides to emancipate herself from her parents.

**You Debate** *In this situation, can Kirsten emancipate herself from her parents?*

### 11 Rescinding a Contract

Matthew is 17, a senior in high school, and in JROTC. A recruiter visits his school to recruit students for the navy. Matthew signs a contract to enlist without discussing it with his parents.

**You Debate** *Since Matthew is a minor and did not discuss this with his parents, can he rescind the contract?*

### 12 Contract for Necessaries

Jordan is 16. While mowing his grass, he seriously cut his hand. His neighbor took him to the emergency room where he was treated and released. Two weeks later, Jordan received a bill from the hospital for \$575. Jordan refused to pay the bill.

**You Debate** *Since Jordan is a minor, can he still be held responsible for the hospital bill?*

### 13 Consideration

Shawn offered to paint Margaret's house in exchange for an old car she was selling for \$4,000. Shawn failed to show up to finish painting the house or to contact Margaret. A week later, another person offered to purchase the car and Margaret sold it. The next day Shawn came by to finish painting the house and learned the car had been sold.

**You Debate** *Can Shawn sue Margaret for breach of contract?*

### 14 Option

Malik offered to sell his condo to Gayathri for \$70,000. Gayathri said she did not have the money right now, but would like an option to buy it at a later date. Malik did not specify a time limit on the offer. A month later Malik had the opportunity to sell the condo for \$70,000. Malik informed Gayathri, and she reminded Malik that she had an option with no time limit.

**You Debate** *Is Malik bound by this agreement with Gayathri?*



**Case Study Practice – Olsen v. Hawkins**

**15 A Case of Incompetence?** Hobart Turner purchased a life insurance policy on his own life. He listed Marvin and Mercedes Olsen, his stepson and his stepson's wife, as the beneficiaries on his policy. Three years later, Mr. Turner changed the beneficiary to Charles Hawkins. Mr. Turner died two years later.

The Olsens sued Mr. Hawkins for the money, arguing that Mr. Turner was not competent to contractually change the beneficiary when he did because he was under the effects of alcoholism. There was no evidence that Mr. Turner was either drunk or insane at the time he changed the beneficiary, but he did suffer from chronic alcoholism. A jury agreed with the Olsens and held that Mr. Turner was incompetent when he changed the beneficiary to Mr. Hawkins because of his alcoholism.

*Source: Olsen v. Hawkins, 408 P.2d 462 (Idaho 1965)*

**Practice** Was the jury right in its findings?

## 16 Ethics Application

**Duty to Disclose?** Shadonna typed up a simple agreement between Jonathan and herself for the sale of her computer equipment valued at \$1000. When Jonathan read the agreement, he saw that Shadonna had made an error and typed the amount in at \$100. Shadonna had already signed her name to the agreement without noticing the error, so Jonathan signed it then handed her \$100.

- ◆ Is Jonathan required to point out the error in the amount to Shadonna before signing the contract?

## 17 Internet Application

**Contractual Capacity of a Minor** Diane is 16. She purchased a used car for cash in her name only. She now needs to purchase insurance in order to register her vehicle.



Log on to [glencoe.com](http://glencoe.com) to access a car insurance Web site to determine the procedure for obtaining auto insurance as a minor. What limitations, if any, are in effect for the contractual transaction?



## Reading Connection

**Outside Reading** Go to [glencoe.com](http://glencoe.com) for a list of reading suggestions about contracts.

# How Contracts Come to an End

## BusinessWeek News

### Cleaning Up at the Casino

By Eamon Javers

For years, the law firm Greenberg Traurig and its controversial lobbyist, Jack Abramoff, got huge checks from casino-rich Indian tribes. Now bucks are flowing the other way. In July, sources say, the firm settled with the Saginaw Chippewa Indian Tribe of Michigan for more than \$10 million that the tribe says it was defrauded by Abramoff, who no longer works at the firm, and PR consultant Michael Scanlon. The tribe says they charged “outrageous fees” for work it has no record of receiving. A spokesman for Abramoff says he had no comment, and Scanlon couldn’t be reached. An attorney says the tribe “will not disclose any details related to the agreement.” A spokeswoman at the firm says: “Any settlement or talks are confidential.”

### Flex Your Reading

Efficient critical reading involves being flexible with speed and comprehension. There are several ways of reading critically, and you need to fit a reading style to your needs and to the material.

Go to [glencoe.com](http://glencoe.com) for Flex Your Reading activities, more information on reading strategies for this chapter, and guided practice in reading contracts.





**Delegation of Duties** Contracts that require someone's personal skill and judgment cannot be delegated. *What are some types of jobs that cannot be delegated to someone else?*

# Transferring and Ending Contracts

## What You'll Learn

- ◆ Explain how and when contracts can be discharged.
- ◆ Analyze the concept of performance.
- ◆ Describe the rules that apply to transfers of rights and duties.
- ◆ Understand the difference between delegation and assignment.

## Why It's Important

Knowing when a contract ends is crucial for determining when the rights and duties of the parties terminate.

## Academic Standards

Reading and completing the activities in this section will help you practice the following academic standards:

**Math (NCTM CS2 3)**  
Recognize and apply mathematics in contexts outside of mathematics.

**English Language Arts (NCTE 8)** Use a variety of technological and information resources to gather and synthesize information and to create and communicate knowledge.

## Reading Guide



### Before You Read

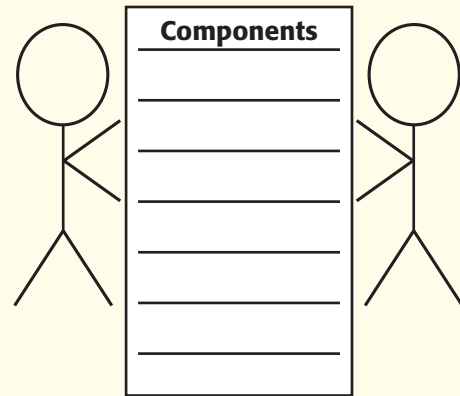
**Connect** If you have signed a contract with someone or with a company, what are the ways this contract could end?

### Focus on Ideas

Contracts may end because all rights and duties have been fulfilled or because the agreement has been broken.

### Take Notes

Create a graph like the one shown and use it to take notes as you read this section. Go to [glencoe.com](http://glencoe.com) to find graphic organizers and tips on how to improve your note-taking skills.



### Key Terms

You will learn these legal words and expressions in this chapter. You can also find these terms in *Black's Law Dictionary* or in an online legal dictionary.

- substantial performance
- tender
- discharge by agreement
- impossibility of performance
- statute of limitations
- breach of contract
- assignment
- delegation



### Academic Terms

You will find these words in your readings and in your tests. Look them up in a dictionary and familiarize yourself with them.

- substituted
- expire
- affected

## Ending a Contract

*If you sign a contract with a personal trainer, and the trainer has an accident and cannot work with you, is your contract still valid?*

A contract is discharged when it comes to an end. The parties to a contract may enforce their rights and must perform their duties, according to the terms of the contract, up to the time of discharge. The law tells us when contracts can end so that people will know when their rights and duties conclude. Contracts can be discharged voluntarily in two ways:

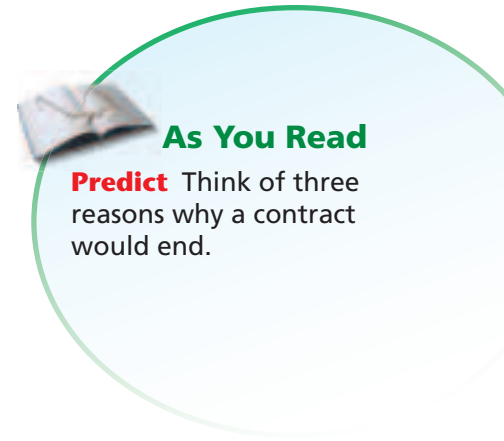
- by performance
- by agreement

### Discharge by Performance

Most contracts are discharged by performance. Performance is a series of activities that fulfills the purpose of a contract. As long as all the terms of the contract have been followed properly and completely, the contract has been discharged. Complete performance represents a stage in the contract at which all the terms have been carried out properly.

**Time for Performance** The time for completing performance may be important to one or both of the parties. If the time for performance is not stated in a contract and there is a question of performance, the court will say that all duties under the contract must be completed in a reasonable time.

Reasonableness is determined by what is suitable, fair, and proper to the goal of the contract. A reasonable time for selling tomatoes, for instance, is not the same as a reasonable time for selling a house.



### As You Read

**Predict** Think of three reasons why a contract would end.

**Time Is of the Essence** A reasonable amount of time to sell produce is not the same as a reasonable amount of time to sell a car. *What are some types of goods or services in which time is of the essence in delivering or selling them?*



If the parties state a time limit in the contract, the court may still give them more time if asked to do so by one of the parties. To avoid any kind of misunderstanding about time, the time limit should be included in the contract along with the words *time is of the essence*.

**Satisfactory Performance** The law requires that contractual services be done in a satisfactory manner. Sometimes, a contract says nothing about satisfaction; at other times, a contract may say that the work must be done in a satisfactory manner. In both situations, when one party believes the job is unsatisfactory, the dispute may end up in court.

In a lawsuit, the court uses the reasonable person test to measure whether the contract was performed in a satisfactory manner. This means the court asks whether a reasonable person would believe that the job was completed in a satisfactory manner. The jury generally gives the answer to this question. If there is no jury, the judge gives the answer. Occasionally one party will agree to perform services to the other party's satisfaction. In such a case, the other party must be satisfied to be held to the contract.

**Substantial Performance** Both parties must fully perform their duties for a contract to end by complete performance. Someone who has not fully performed his or her duties cannot, in most cases, win a lawsuit against the other party for money owed or for other damages.

An exception to this rule is known as the doctrine of substantial performance. **Substantial performance is a situation in which a party has, in good faith, completed the major requirements of a contract, leaving only a few minor details unfinished.** The court will allow that person to recover the amount agreed upon under the contract, minus the cost of completing the job. However, the court will allow recovery only if it can determine that it would be unfair to deny that recovery. The doctrine of substantial performance is often applied to construction contracts.

**Tender of Performance** A party can fulfill the terms of a contract by performing an act or by paying money. A **tender is an offer to do what you have agreed to do under a contract.** It is important to make tender even if you know the other party will not perform his or her part of the contract. In some states, making tender is necessary to test the other party's willingness and ability to perform. If neither party has made tender, then neither party can bring a lawsuit against the other.

If a person who must perform an act makes a tender of performance and that tender is rejected, that person is excused from fulfilling the contract. This principle does not apply to debts. An offer to pay a certain amount to fulfill a contract is a tender of payment. If a person makes a tender of payment and is rejected, that person is not excused from the debt. He or she is only excused from paying further interest on the amount of debt included in the tender of payment.



## Case Study – Opera Co. of Boston v. Wolf Trap Foundation



**Critical Thinking** *If there is an impossibility to perform a contract, who is liable?*



Note key facts in the text below and look up words you do not understand. Restate difficult ideas in your own words. Go back and reread the text quickly to make sure you did not miss any important detail. Now, you are ready to formulate an opinion.

**Impossibility of Performance?** The Opera Co. of Boston and the Wolf Trap Foundation entered into an agreement whereby the Opera Co. would perform an opera for four nights in a row at a theater operated by the Wolf Trap Foundation. In return, the Opera Co. would be paid \$60,000, plus \$53,000 for each performance. The Opera Co. performed on the first three nights without any problems. On the fourth night, however, an electrical storm knocked out power to the theater, and Wolf Trap had to cancel the performance. Because it did not perform, the Wolf Trap Foundation did not give the Opera Co. its final \$53,000 payment. The Opera Co. sued to recover its last payment. Wolf Trap argued that it did not have to make the last payment because the contract was impossible to perform.

*Opera Co. of Boston v. Wolf Trap Foundation, 817 F.2d 1094 (4th Cir. 1987)*



Go to [glencoe.com](http://glencoe.com) for more case study practice.

The person offering to pay the required amount of money must offer legal tender. Under federal law, legal tender for debts, public charges, taxes, and dues is U.S. coins or currency.

### Discharge by Agreement

**Discharge by agreement** means that people can end a contract by mutual agreement. This can be done by mutual release or by accord and satisfaction. A mutual release is an agreement between two parties to end a contract. Whatever the parties agree to do in the first place, they can later agree not to do. Otherwise, there would be no consideration for the promised release. A contract can also be discharged when one party agrees to accept a different performance from the other party. One contract is **substituted** for another. This is called accord and satisfaction. It is often used to settle an honest disagreement on an amount owed.

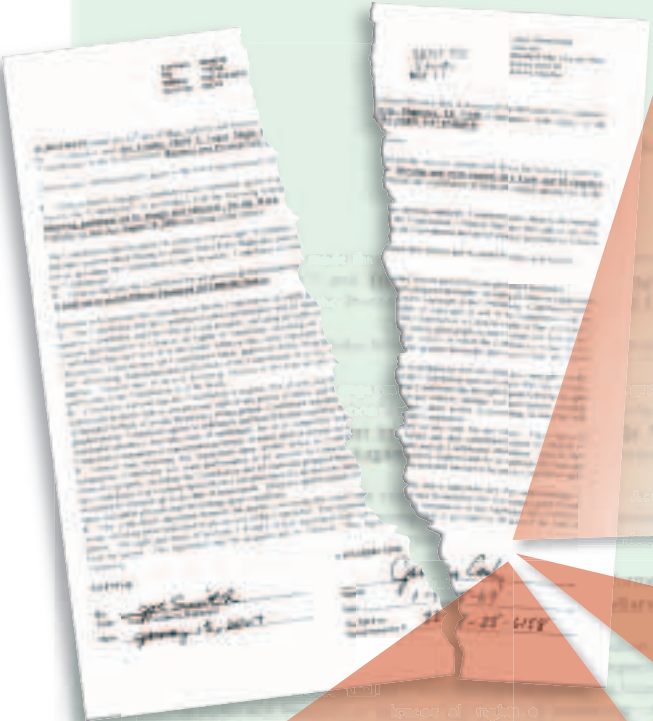
### Involuntary Discharge

Some contracts are discharged involuntarily despite what the parties intend or what they actually do (see **Figure 6.1** on page 135). In these situations, the obligations under the contract may also **expire**. The two primary ways contracts are discharged in this way are:

- by impossibility of performance
- by operation of law

**Vocabulary** You can find vocabulary definitions in the **Key Terms** glossary and **Academic Vocabulary** glossary in the back of this book.

## Figure 6.1 Involuntary Discharge of a Contract




A contract cannot be completed if the subject matter of the contract, such as a piece of property, is destroyed through no fault of the parties to the contract.



The death or illness of a party to a contract may end the contract if it required the personal service of that person.



The law will discharge a contract if the Statute of Limitations for completing the contract runs out.

 Despite what the parties intended to do, some contracts can be ended involuntarily for the reasons shown in the figure. *For what other reasons might an contract be ended involuntarily?*

## Discharge by Impossibility of Performance

A contract that becomes legally impossible to perform generally may be discharged, and both parties may be released from the obligation. The courts allow a discharge for impossibility of performance. **Impossibility of performance may be allowed in case of death or illness that prevents the performance of a personal service contract; the destruction of the exact subject matter, or the means for performance; and illegality, or situations in which the performance of a contract becomes illegal.**

**Death or Illness in a Personal Service Contract** The death or illness of a party to a contract may be an excuse for nonperformance. This is true only if the contract requires the personal service of the person who has died or become ill.

**Destruction of the Exact Subject Matter** If the means or subject matter that is needed to perform the contract is destroyed through no fault of either party, the contract is discharged. The destruction must occur after the contract is entered, but before it is carried out.

## Discharge by Operation of Law

At times, the best interests of society demand that a contract be terminated. Under these circumstances, the law declares contracts discharged by operation of law.

**Wrongful Alteration** One party's wrongful acts (such as altering or changing a contract) will discharge a contract by operation of law.

**Statute of Limitations** State laws specify how much time can pass before you can bring a legal action on a contract. These are called statutes of limitations. **A statute of limitations establishes a time limit for suing in a civil case, based on the date when the breach occurred or was discovered.** There are many special statutes of limitations in every state. To protect yourself fully in important business relationships, you should refer to the most recent statutes in your state. The statute of limitations for failure to perform contracts for the sale of goods is four years in most states. This means a legal action must be begun within four years after the contract is broken.

The parties may reduce the period of limitation to not less than one year by the original agreement. They may not, however, extend the period to more than the limit set by their state. However, a time-out is called when a creditor is a minor or is mentally ill. These situations stop the clock on the statute of limitations. In some states, people who are in prison suffer what is called civil death. They lose the right to vote, to make contracts, and to bring and defend against civil lawsuits. In these states, the statute of limitations on contracts often stops running while a person is in prison.



### Reading Check

**Analyze** What are all the ways performance is looked at when determining if and how a contract may end?




**Debt and Statutes of Limitations** In some instances, the debt may be renewed. If a debtor makes a partial payment or admits that the debt exists after the time period has passed, the debt is renewed for another time period set by the state statute. In New York and some other states, such a new promise must be in writing.

**Bankruptcy** Congress has the authority to pass bankruptcy laws that set procedures for discharging a debtor's obligations. These obligations still exist, but the debtor cannot be imprisoned for failure to pay.

Certain debts cannot be discharged under bankruptcy laws. Education loans, for example, usually cannot be discharged during the first five years of the repayment period. In addition, debts for taxes, alimony, child support, and maintenance are not **affected** by a general discharge of debts in bankruptcy.

## Breach of Contract

*Suppose you advertise your aunt's Picasso painting online, and someone buys it immediately. Two months later the buyer discovers the painting is a fake. Was this fraud on your part?*

 **Transferring Duties** Sometimes people have to shift some of their work to other qualified parties. *Can the duties of a physical trainer be transferred to another physical trainer?*

A **breach of contract** is when a person fails to perform the duties spelled out by a contract. The effects of a breach vary depending on the case. When a breach of contract happens, one party is injured. The injuries are not physical, but that does not mean that they are not real. The injured party may demand justice.

## The Transfer of Contractual Rights and Duties

*If you signed a contract with a personal trainer, can you be assigned another trainer without a new contract?*

When people establish contracts, they receive rights (benefits) and acquire duties (detriments). Most of the time, people manage their own rights and duties. Sometimes, these rights and duties are moved to someone new. For example, some people give another person their right to receive money because they owe that person money they cannot pay otherwise. Other people take on more work than they can handle and have to shift some of their duties to other qualified parties. The law permits this sort of transfer, with a few exceptions.

## Assignment and Transfer of Rights

**An assignment is the transfer of a right under a contract.**

The general rule about assignments is that people can legally transfer contract rights as long as the contract does not specifically say they cannot. The party who transfers the rights is the assignor; the party who gets the rights is the assignee. The assignee is a third person who is not a party to the original contract.

**Example** Anthony Cuomo entered into a contract with Cathy Michaud to rebuild the front steps of her house for \$1,800. The carpenter was pleased to get the contract because he owed \$1,800 to his landlord, David Brown. Before beginning work, Anthony assigned the right to receive payment for the work to his landlord. When payment was due, Cathy paid the \$1,800 to David Brown directly.


**How Rights May Be Assigned** No consideration is necessary for an assignment to be valid. In most cases, the law does not even say how one party may assign a right to somebody else. However, it is best to put an assignment in writing because an oral assignment can be difficult to prove. Suppose that you owe money to a bank under a contract. Now suppose that the bank decides to assign the right to receive your money to another bank. Would you want to know about that change? Of course you would, and you would want the change in writing so that, when you send the money to the new bank, you know that you are doing the right thing.

**What Rights May Be Assigned** Most rights may be assigned unless the assignment changes the obligations of the other party to the contract in an important way. However, not all assignments are valid. For instance, the right to receive personal services usually cannot be assigned. An assignor can assign nothing more than the rights that he or she possesses. An assignee takes those rights, subject to other people's defenses.

**Example** Suppose that when Anthony Cuomo, from the earlier example, assigned the right to receive the \$1,800 to his landlord, Anthony then did a poor job. Cathy Michaud could raise the defense of a poor job if she were sued by the assignee, who wants to collect the \$1,800.

Rights to the payment of money, such as wages, money owed on accounts, royalties on books, and rights to the delivery of goods are the most common types of rights that are assigned. After the assignment, the assignor no longer has an interest in the right that was assigned. This right now belongs exclusively to the assignee.

Generally, no special form is required to make an assignment. Any words that clearly indicate a person's intent are sufficient. This assignment may be made on a separate paper, or it may be written on the back of a written contract containing the rights to be assigned.

 **Third Parties** The make-up artist is putting finishing touches on a character from the movie *Judge Dredd*. Teachers, writers, and artists are selected to perform certain services because of their particular skills or talents. *In the context of rights, transfers of rights, and duties, do you think a chef you hired to oversee the catering of a dinner party could delegate the work to another cook?*



## Delegation and Transfer of Duties

**Delegation** means transferring of a duty under a contract. A delegation should not be confused with an assignment. An assignment is a transfer of rights; a delegation is a transfer of duties. In a transfer of duties, a party to a contract trusts another person to do the job in his or her place.

**Example** Ivan Remec, owner of the Eastern Print Shop, had overextended himself financially and could not meet all of his printing contracts. When the time came to print the monthly newsletter for the high school's Parent Teacher Association, he transferred his contract obligation to another printer who was not a party to the original contract. This was a legal form of subcontracting. However, if Ivan had told the PTA that he would personally do the printing, Ivan could not have delegated the task.

It is important to remember that the performance of an obligation may be delegated, but the responsibility for it may not. If both parties understand the situation, it is all right to hand over the duty of doing the work to someone else. This is a form of subcontracting that is common in business contracts. You may not delegate duties, however, in any of the following situations:

- A party agrees to perform the service personally.
- The contract calls for the exercise of personal skill and judgment.
- The contract itself prohibits delegation.

The offeror and the offeree may include in their contract a statement that the contract may not be assigned or delegated. In this case, both parties are restrained.

If you have the right to delegate a contractual obligation and decide to do so, choose your third party carefully. As explained, you retain responsibility for any job duties that you subcontract or assign to a third party.

**Novation** You do not need the permission of the other party to assign contract rights or to delegate duties to a third person. If you do receive permission, and the other party agrees to deal with the assignee, the resulting contract is called a novation. A novation is an agreement whereby an original party to a contract is replaced by a new party. The other terms of the new contract generally remain the same as those in the original contract. To be effective, the change requires the consent of all of the parties involved.

**Third Parties** A contract is a binding agreement that establishes a relationship between the parties to the contract. This relationship between the parties is termed privity of contract. It determines who can sue whom over a question of performance required by a contract. Usually the parties to a contract have standing to sue.

A third person may sometimes enforce a contract when it is made specifically for that person's benefit. A person who is not a party to a contract but still benefits from the contract is called a third party beneficiary.



### After You Read

**Summarize** List ways you could get out of a contract to sing at your school's football game.

## SECTION 6.1 ASSESSMENT

### Self Check

1. How can contracts be discharged by performance?
2. What situations permit a contractual discharge by impossibility of performance?
3. What situations permit a contractual discharge by operation of law?

### Academic Connection

**Mathematics** Last week, Cynthia used a credit card to purchase a snowboard for \$277.89. This week, she saw the same snowboard on sale online for \$250.43. The sales tax in Cynthia's

state is 8%. The online store is not based in her state and charges only for shipping. Shipping charges are 2% of the item's price. How much would Cynthia save if she could return her snowboard for a refund and order the one she saw online?

**CONCEPT** **Numbers and Operations: Calculating Percentages and Comparing Prices**

Calculate 8% of \$277.89 by multiplying the price by 0.08. Add the result to the price of the snowboard. Calculate shipping charges by multiplying \$250.43 by 0.02. Add the

result to the price. Compare the two results to make a decision.



For more math practice, go to the Math Appendix.

### Critical Thinking Discharged or Not?

Debra agreed to work for Lupe for two years. At the end of two months, Debra went to Lupe and asked to be released from her contract. Lupe agreed. Was the contract discharged? Explain.



Go to [glencoe.com](http://glencoe.com) to check your answers.



# Voidable Contracts and Remedies

## What You'll Learn

- ◆ Differentiate among the ways contracts can be undermined (fraud, non-disclosure, misrepresentation, mistake, duress, and undue influence).
- ◆ Explain what remedies are available when a contract is not fulfilled.

## Why It's Important

Knowing the consequences of a breach of contract can help you prepare for the loss that follows and for deciding on possible recourse.

## Academic Standards

Reading and completing the activities in this section will help you practice the following academic standards:

**English Language Arts (NCTE 4)** Adjust the use of spoken, written, and visual language to communicate effectively with a variety of audiences and for different purposes.

**Math (NCTM CS2 1)** Recognize and use connections among mathematical ideas.

## Reading Guide



### Before You Read

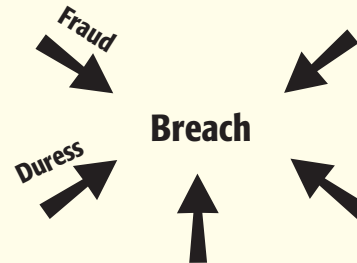
**Connect** Have you ever been pressured into agreeing to do something you did not really want to do? Do you think you should have been able to get out of it?

### Focus on Ideas

A contract can be breached either intentionally or unintentionally.

### Take Notes

Create a graph like the one shown and use it to take notes as you read this section. Go to [glencoe.com](http://glencoe.com) for tips on how to improve your note-taking skills.



### Key Terms

You will learn these legal words and expressions in this chapter. You can also find these terms in *Black's Law Dictionary* or in an online legal dictionary.

- fraud
- duress
- undue influence
- remedy
- damages
- punitive damages
- injunction



### Academic Terms

You will find these words in your readings and in your tests. Look them up in a dictionary and familiarize yourself with them.

- intent
- exaggerate
- mutual

## Defective Agreements

*If a contract appears to meet the requirements of offer, acceptance, agreement, consideration, capacity, and legality, what could still prevent the contract?*


Sometimes, what seems to be a valid contract turns out to be nothing of the kind. In these cases, the agreement is defective. Several circumstances might lead to this situation: fraud, misrepresentation, mistake, duress, and undue influence.

### Fraud

**Fraud** is a deliberate deception intended to serve an **unfair and unlawful gain**. If you figure out that the seller lied, then you may be able to get your money back. That means you may have to sue for money damages. Lying weakens the entire world of contracts, therefore the law will let the injured party get punitive damages. To win a lawsuit based on fraud, five elements must be shown:

- There must be a false representation of fact (a lie).
- The person who lied must know it was a lie.
- The lie must be made with the **intent** that it be relied on.
- The innocent party must reasonably rely on the lie.
- The innocent party must experience a loss.



 **Victims of Fraud** Anybody can become a victim of fraud. *Why do unscrupulous telemarketers often target retired Americans for fraud?*

### As You Read

**Predict** What are some reasons why a contract may be voidable?

**Vocabulary** You can find vocabulary definitions in the **Key Terms** glossary and **Academic Vocabulary** glossary in the back of this book.

## **BellSouth Communications System, LLC v. West**

*902 So.2d 653 (Ala. 2004)*

BellSouth is an Internet Service Provider in Alabama, where Thomas West resides. In 2002, Mr. West signed up with BellSouth for Internet service. The advertised price was \$15.95 per month. When Mr. West received his bill from BellSouth, he discovered he had been charged \$19.85 for one month's service and a \$15.00 set-up fee. Mr. West sued for breach of contract. BellSouth countered, arguing that the membership agreement that Mr. West had signed said that BellSouth could change any terms of the agreement (including the monthly fee) by posting notice on the Internet. Mr. West said he never saw the posting.

### **Ruling and Resolution**

The Alabama Supreme Court held that BellSouth could not provide proof of when it had posted the change in fees on its Web site. Neither could BellSouth prove that Mr. West had accessed the Web site after the alleged change. Therefore, Mr. West was able to recover damages against BellSouth.

**Critical Thinking** Should companies be allowed to notify customers of changes to their contracts by posting notices on Web sites?

**False Representation of Fact** The law requires that the lie be about a material fact that is really important. It cannot be a promise of something that will happen in the future, and it cannot be just an opinion. The law allows sales people to **exaggerate** their claims just as long as the exaggerations are obviously a statement of the seller's opinion.

In the context of fraud, a lie is not just something false that is written or spoken. It can also be actions that the seller uses to cover up a defect or to hide some factual piece of evidence. If your friend, Phil, tells you that he is going to turn back the odometer of his '65 Mustang so he can get a better price for it, you should let him know that he is about to commit fraud. Sometimes people lie by inaction. This happens when they do not say something that they are supposed to say. This is called passive fraud, concealment, or nondisclosure.

**Knowledge of the Lie** To be responsible for the lie, the person telling the lie must know that it is a lie. The innocent party has to show this by giving evidence in court that the other person had actual knowledge that he or she was lying. Short of this, the innocent party might succeed in the lawsuit by showing that the other party told the lie recklessly. This means that the defrauding party told the lie without regard for the true story.

**Lie Intended to Be Relied Upon** To prove fraud, the innocent person must show that the liar told the lie knowing that the other party, would hear it, believe it, and act on it. In other words, he or she told the lie to tempt the other party into the false contract.

**Lie Actually Relied Upon** To prove fraud, the innocent party has to show that he or she depended on the lie. Sometimes the defrauding party lies, but the other party pays no attention to the lie. If that happens, there are no grounds for a lawsuit.

**Resulting Loss** You can be enticed into a contract by a lie that the other party knows is a lie, and you still might not be able to recover damages in court. This happens if the last element is missing. If the innocent party does not lose anything in the deal, there is no loss, and with no loss, there is no fraud.

## Innocent Misrepresentation

Misrepresentation occurs when a person who is involved in contract negotiations says something that he or she believes to be true that turns out to be false. The law gives the innocent party the right to get out of the contract in this situation.


## Mistake, Duress, and Undue Influence

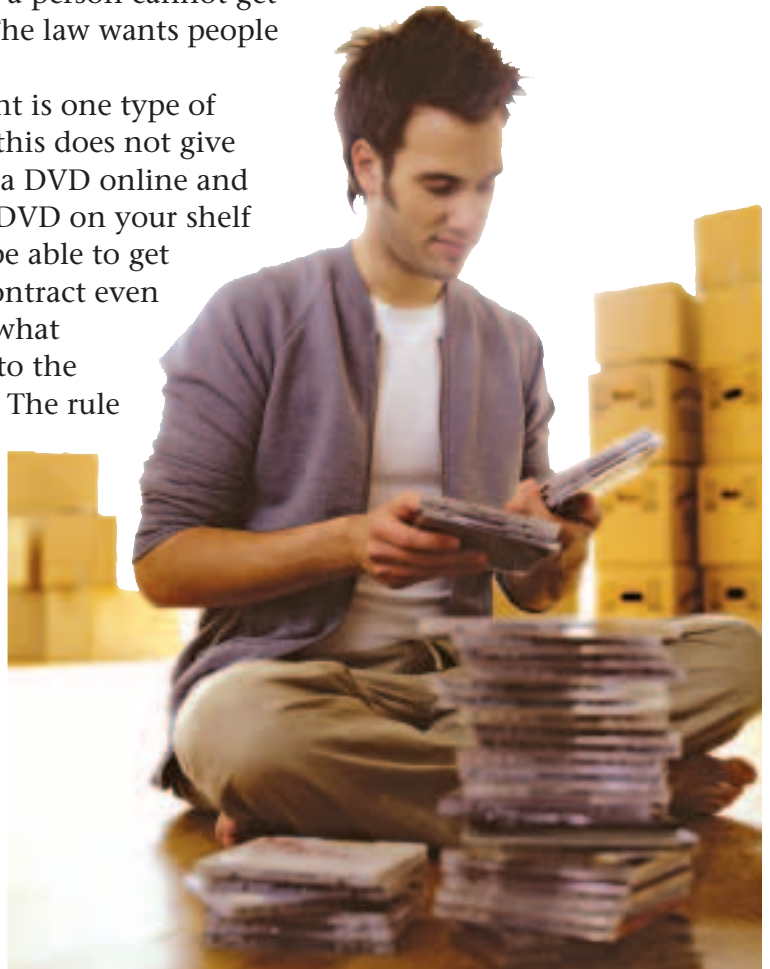
Sometimes a person enters a contract with a mistaken idea of what is at stake. Later, when the mistaken person realizes that an error has been made, he or she tries to get out of the agreement. Is this possible? Sometimes the answer is yes, but more often it is no.

**Unilateral Mistake** A unilateral mistake is an error on the part of one of the parties to the contract. Usually a person cannot get out of a contract just because of a mistake. The law wants people to pay attention to their business deals.

A mistake as to the nature of the agreement is one type of unilateral mistake. A unilateral mistake like this does not give anybody a way out of a contract. If you buy a DVD online and then find out that you have the exact same DVD on your shelf at home, you made a mistake. You will not be able to get out of the contract. People are bound to a contract even if they do not read it or are mistaken about what it says. Your signature shows that you agree to the terms whether you understood them or not. The rule applies even to those who cannot read English. People who cannot read English are expected to have someone who does understand the language read and explain the terms in the agreement.

A mistake as to value (about how much an object for sale is worth) is another type of unilateral mistake. It does not give anybody a way out of a contract.

 **Unilateral Mistake** If you mistakenly buy a CD you already own, you cannot simply negate the contract. *What can you do to avoid this situation?*





**Duress:** *n* Unlawful threat or coercion. From Latin *durus* = hard.

**Punitive:** *adj* Relating to punishment. From Latin *punitus* = punish.

**Vocabulary Builder** List and define three words that have a similar meaning to duress.

**Look It Up!** Check definitions in *Black's Law Dictionary* or an online glossary. For direct links, go to [glencoe.com](http://glencoe.com) to find more vocabulary resources.

**Bilateral Mistake** A bilateral mistake is an error that is made on the part of both parties to the contract. This is also called **mutual** mistake. Often when the mistake is bilateral, either one of the parties can get out of the contract.

A bilateral mistake can be made as to the possibility of performance. This will get rid of the duty to perform. Suppose that you agree to pay your local bookstore owner \$10 if he makes sure that you are the first person to buy the next Harry Potter novel. Now, suppose the author of the Harry Potter books says that she will never write another Harry Potter book—ever. Both you and the book dealer were mistaken as to the availability of a new Harry Potter book. The contract cannot be performed and the agreement is ended.

Suppose you believe you are buying the 2005 VHS version of *The Fantastic Four* feature film. When the tape arrives, you realize that the tape is actually the 1993 film. This is a bilateral mistake as to the subject matter. You were buying the 2005 version while the other party was selling the 1993 version. If the seller was selling one thing while the buyer was buying another, either party can void the contract.

## Duress

**Duress** is the act of destroying somebody's free will by force, threat of force, or bodily harm. Agreements made under duress are either void or voidable.

**Physical Duress** When actual physical force is used to cause another person to enter a contract, the contract is void. When the threat of force is used, the contract is voidable. The threat can be against the person entering the contract or a family member of that person.

**Economic Duress** Economic duress is an act that threatens a person's income or business that makes that person enter a contract without real consent. To succeed in voiding a contract based on economic duress, the victim has to prove three things:

- The other party wrongfully placed them in a poor economic position.
- The victim had no choice other than to submit to the duress.
- Their submission to the duress was reasonable under the circumstances.

## Undue Influence

**Undue influence** is an action or series of overly persuasive actions that make inappropriate use of one person's position of power over another person to create an agreement that is very favorable to the person with all the power. To succeed in voiding a contract based on undue influence, the victim has to prove three things:

- the existence of a caregiver-type relationship
- the use of excessive pressure by the caregiver
- a resulting contract that heavily favors the caregiver

### Reading Check

**Enumerate** What is necessary to prove that fraud has occurred?

## Remedies and Damages

*What do you think you can do if someone has not fulfilled a contract you had agreed to?*

When a contract is not fulfilled, the injured party has a choice of remedies. A **remedy is a legal means of enforcing a right or correcting a wrong**. If you are the injured party, you have three different options:

- You may accept the breach.
- You may sue for money damages.
- You may ask the court for an equitable remedy.

If one party breaches a contract, it is an excuse for the other party not to perform. For example, if someone failed to perform under a contract with you, you may simply accept the breach and consider the contract discharged. This is often the best choice, especially if no damages have been suffered.



## Global Law

### Remedies for Breach of Contract in Japan

**T**he Japanese Civil Code was created in 1896. It was drafted by three private Japanese attorneys. Two of the drafters studied law in France, while the third had studied law in Germany. As a result, the Japanese Civil Code was influenced by both the French Code Napoléon and the German Civil Code. There are also traces of law from English and American sources. The drafters knew it would be almost impossible to base a system of laws on a Japanese common law created by judicial opinions since none existed.

Contract law was implemented in Japan for the first time under the Japanese Civil Code. The Japanese Civil Code includes some provisions that are unlike American contract law. Two major differences are the initial existence of the contract and remedies available for breach of contract.

#### Creation of Contract

In Japan, a contract comes into existence upon the sending of notice of acceptance. For example,

if an offer is made via the mail and the recipient decides to accept the offer, the offer comes into existence the moment the acceptance is mailed. There is no chance to rescind the acceptance. Any rescission would constitute a breach.

#### Remedies for Breach

A remedy for breach of contract is only available if the contract was breached by the obligor, or the person required to perform under the contract. There are no remedies available if the obligee (the beneficiary of the contract) breaches.


#### Across Cultures: The Six Codes (六法 roppō)

In Japan, statutory law originates in the legislature, also called the National Diet of Japan. Under the current constitution, the Emperor may not veto or otherwise refuse to approve a law passed by the Diet.

**Critical Thinking** *Should the United States consider enacting statutory provisions similar to those in Japan?*

**Figure 6.2 Damages**

Type	Description
Actual Damages	An amount of money awarded for damages directly attributable to another party's breach of contract or tort; for example, physician's fees when one party wrongly injures another, and financial losses resulting from failure to deliver goods already contracted for.
Compensatory Damages	An award of an amount of money that compensates a plaintiff for the injuries suffered and nothing more.
Consequential Damages	Damage, loss, or injury (such as loss of profits) that does not flow directly and immediately from the act of the party but only from some of the consequences or results of the act.
Incidental Damages	Reasonable expenses that indirectly result from a breach of contract. They include expenses such as those incurred in stopping delivery of goods, transporting goods, and caring for goods that have been rightfully rejected by a buyer.
Liquidated Damages	An amount of anticipated damages, agreed to by both parties and contained in a contract, to be the basis of any award in the event of a breach of the contract.
Nominal Damages	Damages awarded by a court when a successful plaintiff has proven a legal injury but no actual resulting damages; six cents by common law, usually \$1 today.
Punitive Damages	Damages in excess of losses suffered by the plaintiff awarded to the plaintiff as a measure of punishment for the defendant's wrongful act. Also called exemplary damages because they set an example of punishment awaiting other wrongdoers.
Speculative Damages	Damages not founded on fact but on the expectations that a party may have hoped for from a contract that has been breached; not allowed in any claim for money damages.

 Suing for money damages is one remedy for breach of contract. *What is the objective of awarding damages to the injured party in a contract case?*

## Damages

**Damages** are payment recovered in court by a person who has suffered an injury. (See Figure 6.2.) Damages awarded to recognize a breach of contract that did not cause loss often amount to less than one dollar. These damages are intended merely to recognize that a breach of contract has occurred. Your legal fees for pursuing and winning such a suit would likely far outweigh any damages you would receive.

**Money Damages** If you suffer a loss as the injured party, you may sue for money damages resulting from the breach of contract. The money damages should, by law, place you in the position you would have been in if the contract had been carried out. To recover damages, the injured party must make tender; that is, the injured party must offer to do what he or she agreed to do under the contract.

**Punitive Damages or Rescission** A plaintiff can also receive punitive damages in a lawsuit for fraud. **Punitive damages are money payments for damages that go beyond what the innocent party actually lost and that are designed to punish the wrongdoer.**

If the lawsuit is based on misrepresentation, the innocent party cannot receive punitive damages. The remedy available for innocent misrepresentation is rescission of the contract.

## Equitable Remedies

The remedy of money damages is not always enough to repay an injured party for breach of contract. In these cases, the injured party may seek an equitable remedy. Two chief equitable remedies are specific performance and an injunction.

**Specific Performance** Specific performance asks the court to order the other party in a contract to do what he or she agreed to do. This remedy can only be used when money damages are not sufficient to give relief and when the subject matter of the contract is rare or unique. It would not be ordered in the case of contracts involving common goods or easily obtained services.

**Injunction** An **injunction** is a court order that prevents a party from performing a specific act. An injunction is only available in special circumstances, such as when money damages will be inadequate to compensate the injured party.

An injunction may be temporary or permanent. A temporary injunction is issued as a means of delaying further activity in any contested matter until the court determines whether a permanent injunction should be entered or the injunction should be removed entirely. One who disobeys an injunction does so under penalty of contempt of court.



### After You Read

**Summarize** List all the possible remedies to a breach of contract.

## SECTION 6.2 ASSESSMENT

### Self Check

1. What are the elements of fraud?
2. What are the different remedies for fraud and misrepresentation?
3. What are the requirements of undue influence?

### Academic Connection

**Mathematics** Veronica is considering a short-term commercial loan to expand her business. The amount of the loan would be \$80,000 for sixty days at

an interest rate of 10.5%. To see if this is a good deal, she will need to calculate the interest and the maturity value of her loan.

**CONCEPT** **Number and Operations: Calculating Interest** To solve this problem you will first need to calculate interest using the formula  $\text{Interest} = \text{Principal} \times \text{Rate} \times \text{Time}$ . Maturity value is calculated by adding the principal to the interest owed.



For more math practice, go to the Math Appendix.

### Critical Thinking

**Lying Is Never Worth the Trouble** Suppose you advertised your old laptop computer for sale for \$200. Suppose further that you said it could handle floppy disks when you knew it could not. Suppose further that Jim, the president of the computer club, buys the laptop, sight unseen, relying only on your ad. Have you defrauded Jim whether or not he needs the laptop to handle floppy disks? Explain.

Go to [glencoe.com](http://glencoe.com) to check your answers.



# Chapter 6 Review and Assessment

## Summary

### Section 6.1 Transferring and Ending Contracts

- ◆ When contracts end, they are said to be discharged. The parties to the contract may enforce their rights and must perform their duties up to the time of discharge.
- ◆ When people perform contractual services, the law requires that those services be done in a satisfactory manner.
- ◆ Substantial performance is a situation in which a party has, in good faith, completed the major requirements of a contract, leaving only a few minor details unfinished.
- ◆ Contracts can be discharged by performance, by agreement, by impossibility of performance, or by operation of law.
- ◆ An assignment is the transfer of a right under a contract.
- ◆ A delegation is the handing over of a duty.

### Section 6.2 Voidable Contracts and Remedies

- ◆ When a contract is breached, the injured party has a choice of remedies. A remedy is a legal means of enforcing a right or correcting a wrong.
- ◆ Fraud is an unfair attempt to fool another person into buying something by lying to that person about a key characteristic of the thing that is up for sale.
- ◆ A unilateral mistake is an error on the part of one of the parties to the contract. A bilateral mistake is an error on the part of both parties to the contract.
- ◆ Duress is the act of destroying somebody's free will by force, threat of force, or bodily harm. Agreements made under duress are either void or voidable.
- ◆ Undue influence is an action or series of overly persuasive actions that make inappropriate use of one person's position of power over another person to create an agreement that is very favorable to the person with all the power.

## Vocabulary Builder

1 On a sheet of paper, use each of these terms in a sentence.

### Key Terms

- substantial performance
- tender
- discharge by agreement
- impossibility of performance
- statute of limitations
- breach of contract
- assignment
- delegation
- fraud
- duress
- undue influence
- remedy
- damages
- punitive damages
- injunction

### Academic Vocabulary

- substituted
- affected
- exaggerate
- expire
- intent
- mutual



Go to [glencoe.com](http://glencoe.com) to play a game and improve your legal vocabulary.

**Key Points Review**

Answer the following questions. Refer to the chapter for additional reinforcement.

- 2** Why will the courts allow an innocent party to collect damages in the case of fraud?
- 3** What are punitive damages?
- 4** What types of statements are not fraudulent, even though they might not be 100% accurate?
- 5** Does fraud have to consist of words? Explain.
- 6** What remedy is available in the case of misrepresentation?
- 7** Is a person bound by the terms of an agreement that he or she failed to read? Explain.

**Standardized Test Practice**

- 8** Read the following information about the general rule of law in construction and complete questions 1 and 2.

The general rule of law is that strict performance of the duties of a contract is a condition precedent to recovery on the contract. If that rule were applied to construction, it would mean that owners could refuse to pay for work that did not meet minor quality standards of the contract. For reasons of fairness, building contracts are an exception to the general rule.

In construction, there is the substantial performance doctrine, which says that if the performance nearly equals what was bargained for by the parties, then payment must be made. If the owner can use the work for the purpose that was intended, then the work will be deemed substantially complete, and the owner is obligated to make payment. However, it should be remembered that an owner is permitted to make a reasonable deduction for the cost of achieving full performance.

**1. As a general rule, when must strict performance occur to recover on a contract?**

- A** before final payment is made
- B** at the start of the construction job
- C** at the conclusion of the job
- D** prior to the conclusion of the contract

**2. Why is strict performance defined differently in contracts dealing with construction?**

- A** to be fair to contractors
- B** less contracts would be written
- C** cost of construction would rise
- D** owners would not be obligated to pay

**Test-taking Strategies**

Read the stem of each question carefully, then read each of the possible answers all the way through.



## Apply and Debate

Read the following scenarios. Get together with other students in pairs or groups of three and take a position on each scenario. Debate your position in class with students taking the opposite position or prepare a written argument justifying your position.

### 9 False Representation

Enola was in a collision that caused over \$5,000 in damage to her car. After she had it repaired, she sold the car for \$8,500. The buyer asked Enola if the car had ever been in a major car accident. Enola said no because it had been completely fixed.

**You Debate** *Can Enola be accused of false representation?*

### 10 Implied Contract

While talking to a group of her friends at a picnic, Rosie said she would pay anything to get a tree cut down. The following day while she was at work, one of her friends cut the tree down and gave Rosie a \$500 bill for doing the job.

**You Debate** *Is Rosie required to pay the bill because of her statement the day before?*

### 11 Undue Influence

Jules advertised his motorcycle in the paper for \$2,000. Two people arrived at the same time, and both decided they wanted to buy it. One of them offered \$2,500 for the motorcycle. The other said he could not afford that much, so Jules took the \$2,500 offer. The next day the buyer accused Jules of undue influence for causing him to pay \$500 more for the motorcycle than advertised.

**You Debate** *Did Jules use undue influence?*

### 12 Economic Duress

Mr. Sadri has had his lawn mowed by Ray's Landscaping for \$25 a week for the past three years. Ray's Landscaping told Mr. Sadri that they were raising their fee to \$30 a week. Mr. Sadri threatened Ray's Landscaping that if it did not keep the price at \$25, he would tell his neighbors that Ray's had damaged his flower beds.

**You Debate** *Can Mr. Sadri be accused of duress?*

### 13 Breach of Contract

Sally offered to sell Paco her CD player for \$20. Paco told her he would think about it and let her know later that day. Later, Paco told Sally that he would buy her CD player, but Sally told him she had changed her mind.

**You Debate** *Can Paco sue Sally for breach of contract?*





## Case Study Practice – Parker v. Twentieth Century Fox Film Corp.



**14 What Is a Valid Offer?** Shirley MacLaine Parker and Twentieth Century Fox signed a contract in which Ms. Parker would star in a movie entitled *Bloomer Girl* and she would receive guaranteed compensation of \$750,000 for her performance. The studio decided not to make the movie and notified Ms. Parker of its decision.

To prevent any monetary damage to Ms. Parker, the studio offered her another role in a movie entitled *Big Country, Big Man*. The compensation for the new film would be identical with the compensation offered in the first contract. *Bloomer Girl*, however, was a musical to be filmed in California while *Big Country* was a Western set to shoot in Australia. Ms. Parker was given one week to consider the new offer, which she rejected.

Ms. Parker then sued Twentieth Century Fox for her guaranteed compensation of \$750,000. Twentieth Century Fox argued that Ms. Parker failed to mitigate her damages by refusing to accept the second contract.

Source: *Parker v. Twentieth Century Fox Film Corp*, 474 P.2d 689 (Cal. 1970)

**Practice** Was Ms. Parker required to mitigate by accepting the second offer?

## 15 Ethics Application

**Compensation or Not?** Lukas had contracted Wilson's Roofing to replace the roof on his home. Before they finished the job, Lukas suffered water damage to his carpet from a leak in the roof. To make up for the inconvenience, he decided to claim that his sofa and recliner had also been damaged by water. The company agreed to replace the items immediately and apologized for the mishap.

- ◆ Should Lukas be entitled to any compensation for his inconvenience resulting from the water damage to his carpet?

## 16 Internet Application

**Yearbook Printing** Whitney has a contract with a local printer for her school's yearbooks. When she picks up the yearbooks, she discovers they are filled with errors. The company refuses to reprint the yearbook. Whitney wants to bring a breach of contract suit against them. Research what her options are and which legal principles apply to her situation.



Go to [glencoe.com](http://glencoe.com) to find links and access to reliable Web sites where you can research legal information. Locate and read relevant documents and draft a bullet-point list to advise Whitney on the strategy she could follow.

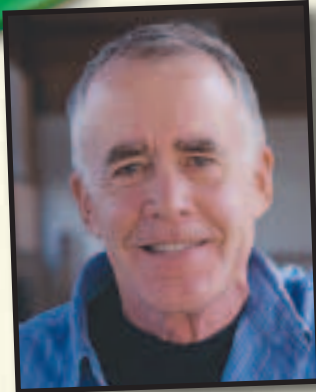


## Reading Connection

**Outside Reading** Go to [glencoe.com](http://glencoe.com) for a list of reading suggestions about contracts.

**Richard Stim**

Editor and General Counsel, Nolo Press



*What do you do at work?*

“I review contracts, modify them, prepare contracts for other businesses to sign, and sometimes negotiate the terms. As an attorney for Nolo, I might get a contract for someone who wants to license materials from us, or a contract for a company that wants to distribute our software in some other configuration. Because we provide legal information, we have to be very careful that we’re not violating any laws that restrict dissemination of legal advice. I deal with several different departments in the building. I might need to review the cover of a book, for instance, to make sure we’re not making claims on the cover that might get us in trouble.”

*What skills are most important to you?*

“Organization is really important. Perspective is important too—you have to be able to see the agreement through the client’s eyes, not just from a legal perspective. The ability to predict problems is pretty important, and another one would be the ability to resolve an impasse.”

*What training do you recommend?*

“For contracts, it really helps to have some business experience, because the biggest problems lawyers have when doing contracts for business clients is that they view all potential disasters as being of equal importance. And that is not the case with most businesses—there is usually one main possible disaster that they are primarily concerned about. Having some business experience is really, really important.”

*What is your key to success?*

“Lawyers are often worried about malpractice, and because they’re so worried about it, it drives them to over-prescribe. And letting go of that is key, wherever you can learn that—and usually you learn that by being in business yourself. Also, if I have any success it’s because I get to know the people and their business. It really helps to understand it, because in the end, it’s never about the paper—it’s always about the people.”

**Résumé Builder**

**Academic Skills**

- Above average reading and writing skills
- Good speaking and debating skills

**Education and Training**

A bachelor’s degree, a Juris Doctor degree, the bar exam in your state. The following high school and college courses will help develop the necessary background knowledge:

- English Language Arts
- Social Studies
- U.S. History
- U.S. Government
- Introduction to Law (in high school)
- Basic law courses (in college)
- Business, contracts, and consumer law

**Critical Thinking**

Why is it important for a lawyer to view a contract from the client’s perspective, as well as from a legal perspective?

 Go to [glencoe.com](http://glencoe.com) to find legal careers resources.

# UNIT 2

## The Writing Connection

### *Persuasive Writing Practice*

**Is There a Contract?** Carmen wants to sell her house. Dale contacts her after meeting her at a party and says she is looking for a house in Carmen's neighborhood. They discuss the matter over the phone. Then, Dale comes over and they reach an agreement on a price of \$300,000. Carmen agrees to fence the yard and to replace the roof as part of the deal. They do not sign a contract. Carmen hires a contractor to do the work. Two days after the contractor has started working, Dale calls to say that she is backing out of the deal because she is being transferred to work in another city. Carmen has spent \$2,000 on the repairs so far.

#### Assignments

**Research** Research which type of contract should be in writing in order to be enforceable by courts, and find out about a law called the Statute of Frauds.

**Write** Consider the situation above and write a persuasive essay about what a fair solution to the situation could be.

**Writing Tips** Before you start writing your essay, read through the following composition review tips:

- ✓ Generate two or three specific sentences that answer the question posed by the assignment.
- ✓ Decide how you will develop your argument.
- ✓ Create an outline.
- ✓ Create a topic sentence for each paragraph.
- ✓ Use transition words at the beginning of each paragraph.
- ✓ Reread, edit, correct, and rewrite as necessary.

**Essay Test Strategies** Preview the essay prompt. Spend five percent of your time reading through the prompt carefully, mark key terms, decide how to budget your time, and jot down brief notes for ideas.



Go to [glencoe.com](http://glencoe.com) to find more writing resources.

**Writing a Driving Contract**

For this project, you will use what you have learned to prepare a written contract that lists issues and responsibilities associated with driving. You can work on this project alone or with a partner.

Here is a checklist of the skills that you will need to complete this project and that your teacher will consider when evaluating your work.

<b>Evaluation Rubric</b>	
<b>Academic Skills</b>	
1. Online and library research	1. 10 points
2. Reading for information	2. 10 points
3. Note-taking	3. 5 points
4. Estimation and computation of your car-related expenses	4. 10 points
5. English composition	5. 15 points
<b>Legal Skills</b>	
6. Research of possible contract forms	6. 15 points
7. Drafting the terms of the contract	7. 15 points
8. Analysis of the essential elements of the contract	8. 15 points
9. Use of technology	9. 5 points
	<b>Total 100 points</b>

 For more resources and for grading rubrics, go to [glencoe.com](http://glencoe.com)

**Step 1: Preparation**

- 1 Write a contract between yourself and a parent or a family member.
- 2 Use all you have learned in this unit, at the library, or on the Internet as tools.
- 3 Complete this project in a format acceptable for a portfolio addition.

## Step 2: Procedure

- 1 **Review** the text in this unit and make a list of the essential elements of a contract. Go to [glencoe.com](http://glencoe.com) to find an appropriate contract form.
- 2 **List** all the contractual terms you might include in your document. What will your obligations be? What will the other party's obligations be? How will these obligations be enforced?
- 3 **Write** the contract based on your knowledge and research. Use the Internet to download a form for an agreement, or create a contract by using word-processing software. Make enough copies so your classmates can review and annotate your contract.
- 4 **Describe** the real-life scenario that is the basis for your contract (the amount of driving you need or want to do, the insurance contract, who the car belongs to, the rules governing teen driving in your state, etc.) and present your contract to the class.

## Step 3: Create an Analysis Report

As a class, compare the contracts presented. Create a spreadsheet that describes the types of agreements created (for example, indicate whether the contracts are unilateral or bilateral) and the responsibilities involved. Make sure that you have also accounted for each of the elements required for a valid and enforceable contract. Look at the charts your classmates have created and answer the following questions:

- 1 How many and what types of contracts were presented?
- 2 Did all of the contracts presented include all the necessary elements?
- 3 If not, how did the absence of the element(s) affect the contract(s)?
- 4 How was your contract similar to and different from the other contracts presented?



### Community Connection

Find statistics about teen driving offenses and accidents online. How do these facts relate to your contract project? Should teen driving offenses be handled in teen or youth courts? Prepare a brief research report to present in class. Go to [glencoe.com](http://glencoe.com) to find resources.



### Competitive Event Prep

#### Entering into Contracts

**Situation** Assume you are a sales associate for a cellular phone store. Besides selling cell phones, your store sells service contracts. You completed a sale to a teen-aged customer (event judge) for a phone and a contract. You checked the customer's identification and discovered that the customer is only 16 years old. Company policy states that any customer under 18 must have a parent or guardian sign the cell phone activation contract.

**Activity** Explain to your customer (event judge) that he or she is under the legal age to sign a contract and must bring a parent or guardian into the store to sign.



For more Competitive Event preparation, performance tips, and evaluation rubrics, go to [glencoe.com](http://glencoe.com).





## **Mastrobuono v. Shearson Lehman Hutton, Inc.**

*United States Supreme Court 514 U.S. 52 (1995)*

**Read Critically** As you read this case, ask yourself the following questions:

1. What type of contract is involved in this case?
2. Why did Shearson Lehman Hutton force the Mastrobuonos to participate in arbitration?
3. What does a court attempt to determine when it interprets a contract?

**Assignment** When you are done, write a short summary of the situation. Include the court's decision and a couple of sentences about why or how the court reached its decision.

**Facts Terms of the Contract** Antonio Mastrobuono and his wife started an investment account at Shearson Lehman Hutton, Inc. When they opened their account, the Mastrobuonos signed a contract provided by Shearson Lehman Hutton. The contract required that the parties arbitrate any disputes that might arise. The contract also contained a provision stating that it would be governed by New York state law. In an arbitration proceeding, the parties present their dispute to an impartial third person or panel and agree to abide by the arbitrator's lawful decision. Because arbitration is considered less time consuming and less costly than litigation, many contracts contain a provision in which the parties agree that disputes be resolved through arbitration.

**Arbitration or Court?** For a variety of reasons, the Mastrobuonos became dissatisfied with the investment services they received from Shearson Lehman Hutton. They closed their account and sued Shearson

Lehman Hutton, alleging that their account had been mismanaged. Because of the contract's arbitration provision, Shearson Lehman Hutton suspended the litigation and forced the Mastrobuonos to go before a three-member panel of arbitrators. The panel awarded the Mastrobuonos compensatory damages of \$159,327 and punitive damages of \$400,000. Compensatory damages are awarded to compensate an injured party for actual losses. Punitive damages may be awarded in limited circumstances to punish a person or company for wrongful conduct. Punitive damages are also awarded to prevent other companies from behaving in a similar unlawful or unethical manner. In many cases, the threat of suffering financial loss by way of punitive damages will discourage a company or individual from engaging in unscrupulous behavior. Shearson Lehman Hutton paid the compensatory damages but obtained a court order vacating the award for punitive damages because New York law permits only courts to award punitive damages.

## Opinion Different Interpretations

The Court observed that the contract between the parties in this case contained no express provision about punitive damages. Because the parties agreed to arbitrate a dispute, the Mastrobuonos claimed that the parties were bound by the arbitration panel's decision. Shearson Lehman Hutton argued that the contract limits the matters that may be arbitrated because the parties agreed that the contract would be governed by New York law, which only authorizes courts to award punitive damages. As a result of these differing views, the Court had to interpret the meaning of the contract.

### Determining the Intent of the Parties

The Court said that when interpreting a contract, it must determine the intent of the parties at the time that they entered into the agreement. The original intent of the parties would be used to guide the court's decision. In this contract, the parties agreed that arbitration would be conducted in accordance with rules of the National Association of Security Dealers (NASD), which states that arbitrators may award "damages and other relief." The NASD manual further provides that "No agreement [between a member and a customer] shall include any condition which... limits the ability of a party to file any claim in arbitration or limits the ability of an arbitrator to make any award." However, the contract also states that it is governed by New York law, which permits only courts to award punitive damages. These conflicting provisions create an ambiguity in the contract.

### Ambiguous Terms

Under common law, ambiguous terms in a contract are interpreted against the party that drafted the contract. Ambiguous terms can be understood in different ways. This view of ambiguity protects the party who did not prepare the contract. A party that

had no input in drafting a contract cannot be blamed for that contract's ambiguities. As stated in the Restatement (Second) of Contracts § 206, Comment a (1979):

*"Where one party chooses the terms of a contract, he is likely to provide more carefully for the protection of his own interests than for those of the other party. He is also more likely than the other party to have reason to know of uncertainties of meaning. Indeed, he may leave meaning deliberately obscure, intending to decide at a later date what meaning to assert. In cases of doubt, therefore, so long as other factors are not decisive, there is substantial reason for preferring the meaning of the other party."*

Because Shearson Lehman Hutton prepared the contract for the Mastrobuonos' signatures, any ambiguity must be interpreted in favor of the Mastrobuonos.

**Holding The Court's Decision** The contract between the parties is ambiguous. Under well-established rules of common law, ambiguities in a contract are construed against the party who wrote the contract. As a result, the arbitration panel's award of punitive damages was upheld.

## TRIAL PREP

The National High School Mock Trial Association organizes competitions at the local, regional, and national levels where teams of high school or college students prepare and argue fictional legal cases before practicing attorneys and judges. Mock Trial team members are each assigned a role as either an attorney or witness. Each team must develop a courtroom strategy, legal arguments, and a presentation style.



Go to [glencoe.com](https://www.glencoe.com) to find guided activities about case strategy and presentation.