

## Contracts – Offer & Acceptance

**Contract** (“K”) – an agreement between two parties that courts will enforce (Ks are the basis for all economic activity in a market economy). There are 5 elements required to form a K:

1. **Offer & Acceptance** – a serious, definite offer to contract; accepted by person offered to
2. **Genuine Agreement** – not based on deceit, an important mistake or unfair pressure
3. **Consideration** – both sides must receive something of value
4. **Capacity** – must be able to contract legally (minors, insanity, intoxication)
5. **Legality** – must be legal (can’t pay someone to commit crime or tort)

**Offer** – a proposal by an offeror to do something, provided the offeree does something in return (if the offeree accepts the proposal, a contract arises). There are 3 elements of an offer:

1. **Expression of intent to create a legal obligation** (offeror must appear serious)
  - Test of the reasonable person (how a reasonable person would *interpret* conduct)
  - Facts & circumstances (words spoken as a joke, in anger, etc. – not an offer)
  - Social agreements (when people make arrangements or dates, these are not Ks)
2. **Offer must be complete & clear** (court must be able to determine what parties intend)
  - Complete (needs all essential info: usually price, subject matter and quantity)
  - Clear (each essential term must be identified clearly)
  - Advertisements (usually treated as invitations, not offers)
3. **Offer must be communicated to the offeree** (person who is not the intended offeree or who is unaware of the offer cannot accept the offer)

**Termination of Offers** – offers do not last forever. There are 6 ways to terminate an offer:

1. **Revocation by the offeror** (offeror may revoke an offer anytime before it is accepted)
2. **Time stated in the offer** (offeror may specify how and when the offer must be accepted)
3. **Reasonable length of time** (stays open for a reasonable amount of time)
4. **Rejection by the offeree** (when offeree rejects the offer, it is terminated)
5. **Counteroffer** (if offer is not accepted exactly, a counteroffer is made and original offer is rejected)
6. **Death or insanity of either party** (no longer able to enter into contract)

**Keeping an Offer Open** – an offeror has no obligation to keep an offer open for a specified time even if he has promised to do so. There are 2 ways to keep an offer open, however:

1. **Option** (offeree gives the offeror something of value in return for a promise to keep the offer open – options are not canceled due to death or insanity of one of the parties)
2. **Firm Offer** (special rule that applies to *merchants* must be in writing)

**Acceptance** – acceptance occurs when a party *to whom an offer has been made* agree to the proposal. To create an enforceable contract ... the acceptance must:

1. **Be made by the person to whom the offer was made.**
2. **Match the terms in the offer.** Mirror image rule (must be identical, with exception for merchants)
3. **Be communicated to the offeror.**
  - Silence as acceptance (you are never obligated to reply to offers made by others ... unless both parties have agreed that silence will be assumed to be acceptance)
  - Unilateral acceptance (Ks requiring the offeree to perform certain actions as their acceptance of the offer are considered unilateral contracts ... only one party must perform)
  - Bilateral acceptance (Ks requiring both parties to perform certain actions ... accepted with promises by both parties ... promise of payment for promise to paint the fence)

**Timing** – offers and terminations are effective when *received*; acceptances are effective when *sent*

## Contracts – Genuine Agreement

**Genuine Agreement** – without duress, undue influence, mistake, misrepresentation or fraud.

1. If there was not genuine agreement, the contract may be voidable. This means the injured party has the option of **rescission** (backing out of the transaction by returning what was given).
2. Rescissions must be *prompt* and must take place before **ratification** (acting like you want to live with the K, like by paying the first installment of your loan)

**Duress** – when one party to a contract uses an improper threat or act to obtain an expression of agreement. The important issue is the nature of the threat:

1. **Threats of illegal conduct.** threat to engage in illegal conduct (**crime or tort**) is always duress.
2. **Threats to report crimes.** Coercing someone by threatening to report their crimes (extortion)
3. **Threats to sue.** Using the threat of a lawsuit to coerce someone into an agreement.
4. **Economic threats.** Threat of economic (\$) consequences

**Undue Influence** – when one party to a K is in a position of trust & wrongfully dominates the other.

1. **The Relationship.** A relationship of *trust*, confidence, or authority must exist between parties. May be a formal relationship (teacher-student) or an informal relationship.
2. **Unfair Persuasion.** If dominant party to contract receives unfair terms, then undue influence may exist (and the dominated party may rescind)

**Mistake** – when one or both parties are mistaken about facts of K:

1. **Unilateral Mistakes** – when *one* party holds an incorrect belief about the facts related to a K
  - Innocent unilateral mistake (if someone fails to read K carefully before signing ... K is still valid)
  - Recognized unilateral mistake (major mistake that other party is *aware* of ... K is voidable)
  - Induced unilateral mistake (one party *encouraged* other to make the mistake ... K is voidable)
2. **Mutual (Bilateral) Mistakes** – when *both* parties have incorrect beliefs about an important fact; important facts that influence parties' decision making about a K are called material facts
  - Mistake about subject matter. (mutual mistakes of fact ...K is void)
  - Mistake of law (mutual mistake about applicable laws ... K is still valid)

**Misrepresentation** – statements that turn out to be untrue may be either *innocent* or *fraudulent* misrepresentation ... both of these defenses make the K voidable. 3 elements of misrep:

1. **Untrue Statement of Fact** (in misrep, the statement must be one of *fact* ... a *past* or *existing* fact ... otherwise it is just an *opinion*; opinions of experts are considered to be statements of fact)
  - Active Concealment: same as a false statement of fact.
  - Silence: in many situations the seller may remain silent about defects, *except*: (i) if you make a statement about a material fact that omits important info; (ii) if a true statement is made untrue by subsequent events; or (iii) if one party knows other has made a basic mistaken assumption.
2. **Materiality.** Untrue statements may be considered material if: (i) statement would cause a reasonable person to contract; (ii) they knew the other person would rely on the statement; or (iii) they knew the statement was false.
3. **Reasonable Reliance** (the victim *must* have reasonably relied on the untrue statement)

**Fraud** – fraud is *based* on misrepresentation ... all the elements of misrep must be proven or there is no fraud). In addition to misrep, 2 additional elements must be proven to show fraud:

4. **Intent** (misrep must be intentional or reckless: (i) deliberately lying or concealing a material fact; or (ii) recklessly making a false statement of fact w/o knowing whether it is true or false)
5. **Injury** (misrep or concealment must injure – proof of injury must exist to establish fraud)

**Remedies for Fraud** – as with misrep, rescission is a remedy ... but with fraud, compensatory and punitive damages are also possible remedies

## Contracts – Consideration

**Consideration** (main purpose is to distinguish between social promises and more serious transactions where one thing is being exchanged for another).

1. **Act, Forbearance or Promise.** Each party must give an *act, forbearance* or *promise* to the other.
2. **Trading.** Consideration must be *mutual* ... each party must trade what they contribute to the transaction (act, forbearance or promise) for the other party's contribution: "if you do this for me, I'll do that for you" [promisor & promisee] ... if one does not give consideration, the other has no duty
3. **Legal Value.** What each party trades must have legal value – worth something in eyes of the law. Legal value is found in the exchange of: 2 benefits ... a benefit for a detriment ... or 2 detriments  
- examples: (2B) being paid to mow lawn; (B-D) being paid to quit smoking; (2D) I'll quit if you quit

**Adequacy of Consideration.** generally, what parties give and get as consideration do not need to be of equal economic value ... economic value is unimportant if there is genuine agreement. A big gap may indicate a lack of genuine agreement ... if grossly unfair, court may declare unconscionable

**Nominal Consideration.** may have in a contract consideration of \$1 (or some other nominal amount) because (i) it is difficult to express true value or (ii) do not want to publicize real value

### PROBLEMS with Consideration

**Illusory Promises** (contracts with escape clauses ... no real obligation ... no consideration)

example: you promise to paint your neighbor's house – if you have time (not binding)

- Termination Clauses (often, businesses want the ability to withdraw from a contract if business circumstances change ... ok, as long as it isn't "for any reason")

**Existing Duty** (promising to do something that you are *already obligated* to do by law or prior contract cannot serve consideration ... no real obligation ... no consideration)

- Existing Public Duty (if the law creates a duty to do (or not do) a certain thing, this duty cannot be the basis of consideration in a contract)
- Existing Private Duty (if a prior contract creates a duty, this duty cannot be the basis of consideration in a future contract)

**Mutual Gifts** – consideration on both sides must be traded one for another ... if they are not traded, then there are probable two gifts being made

**Past Performance** – an act that has already been performed cannot serve as consideration!

### EXCEPTIONS to Consideration Requirement

**Promissory Estoppel** – when someone intends a gift but consideration is not present, a promise may be enforced under the doctrine of promissory estoppel. These conditions must be met:

1. Promisor should reasonably foresee that the promisee will rely on the promise
2. Promisee does, in fact, act in reliance on the promise
3. Promisee would suffer a substantial economic loss if the promise is not enforced
4. Injustice can be avoided only by enforcement of the promise

**Promises to Charitable Organizations** (courts generally enforce these) No Consideration Needed.

**Firm Offers** (a merchant that agrees in writing to keep an offer open) No Consideration Needed.

## Contracts – Capacity

**Capacity Rights** (two basic protections granted to those who lack capacity)

Necessaries (things needed to maintain life and lifestyle –food, clothing, shelter, transportation ... can vary from one person to another)

- Minors pay only fair market value

Non-Necessaries (things that for them are relative luxuries)

- Minors pay the contracted price, but the protected party has the option to disaffirm the contract

**Disaffirmance** (non-necessaries: involves giving back the consideration by both parties)

Period of Minority - Minors may disaffirm contracts for non-necessaries during their minority

Period of Majority - After achieving majority, may disaffirm contracts for a “reasonable period of time”

Ability to disaffirm after majority is immediately cut off if the person ratifies contract

**Ratification** (acting toward the contract as if they intend to be bound by it)

**Emancipation** (severing of the child-parent relationship ... ends the duty of the parent to support a child and duty of the child to obey the parent) – treated differently in different states

1. Minor reaches age of majority (occurs naturally when the child attains age of majority)
  - If minor turns 18 while still in HS, then parents still responsible until graduation
2. Marriage of minor (not becoming a parent, however)
3. Minor joins armed forces
4. Court decree: [NOT AVAILABLE IN OHIO]

### Time of Disaffirmance and Ratification

**Disaffirmance.** Parties lacking capacity may disaffirm a contract for non-necessaries:

1. any time *while still under* the incapacity, or
2. within a *reasonable time after* attaining capacity

**Ratification** (action by party indicating intent to be bound by K) may take place *after* party attains majority and may consist of either of the following:

1. giving a new promise to perform as agreed
2. any act that indicates the party’s intent to be bound

### Return of Goods or Services

When a minor disaffirms a contract, anything of value must be returned by them, and then they must get back whatever they gave. (if minors are unable to return exactly what was received under the contract they can still get back everything they gave)

### Obligations of Party with Capacity

While the party lacking capacity may disaffirm contracts, they may also choose to enforce the contract against the other party (and the other party must abide by contract)

**Contracts That Cannot Be Disaffirmed** Exceptions vary state by state. Common exceptions:

- Court-approved contracts (once approved by courts, may not be disaffirmed)
- Major commitments (enlisting in armed services, educational loans and marriage)
- Banking commitments (savings deposits/withdrawals) / Insurance contracts
- Work-related contracts (if minor has own business)

### Misrepresenting Your Age

Minors occasionally may misrepresent their age when entering into a contract

- these minors *may* still be able disaffirm their contracts, but minors who give false ages may be held liable for the tort of fraud and can be sued for damages in court!