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## Contracts

Walter W. Theus Jr.

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# CONTRACTS

## I. OFFER AND ACCEPTANCE

In *Cain v. Noel*,<sup>1</sup> the South Carolina Supreme Court was presented with a question of basic contract law: can an offer containing no explicit termination date be revoked by a general deadline for all offers contained in prior correspondence between the parties? The court did not, however, decide the case on the issue as framed in the briefs of the parties. Instead, it adopted its own theory and the logic of the resulting opinion is questionable.

The litigation arose from negotiations between plaintiff Cain, Chief School Administrator of Edgefield County, and defendants, members of the School Board of Edgefield County. The negotiations concerned plaintiff's continued employment by the Board. On June 20, 1975, plaintiff offered to resign in exchange for a full year's pay. The following day he received a letter from the Board rejecting his offer. This letter concluded: "In any event, the alternative mentioned above, or any other alternative, will be terminated by the Board after twelve o'clock, noon, on Friday, June 27, 1975. . . ."<sup>2</sup> On June 26 plaintiff received a written proposal offering to pay him six months salary in return for his resignation. On June 30, he delivered to defendants his resignation and a letter explaining that he was responding to the offer of June 26. Later that evening, defendants telephoned plaintiff, stating that the Board accepted his resignation, but refused to pay him the six months salary. This conversation was followed on July 3 by a letter from defendants to plaintiff; the letter stated that the Board had accepted the resignation and expressly referred to the June 30 telephone conversation. Alleging that they had breached a contract to pay him the six months salary plaintiff sued the members of the Board. The jury found in favor of defendants. Plaintiff appealed to the supreme court claiming that the trial judge erred in refusing to grant his motions for a directed verdict, a judgment notwithstanding the verdict, or a new trial.<sup>3</sup> The South Carolina Supreme Court reversed and found that the evidence was susceptible to only one reasonable inference. Because that inference supported plaintiff's claim, the judge should

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1. 268 S.C. 583, 235 S.E.2d 292 (1977).

2. Record at 50. "[T]he alternative mentioned above" was apparently that Cain resign immediately, with pay. *Id.* at 12.

3. Brief for Appellant at iii.

have granted the motion for a directed verdict.<sup>4</sup>

The issue raised on appeal concerned common-law principles of offer and acceptance. Basic contract law provides that an offeror is master of the offer, and may place any condition upon its acceptance.<sup>5</sup> In their briefs, the parties argued whether the June 27 deadline should apply to defendants' June 26 offer to plaintiff. Defendants cited general authority that allows the offeror to establish the cutoff point for the power of acceptance.<sup>6</sup> Plaintiff, while acknowledging the validity of this rule, argued that the time limitation was not communicated with sufficient definiteness, and therefore that he had a reasonable time to accept the offer.<sup>7</sup> The court found, however, that plaintiff's resignation and letter of June 30 constituted a counter-offer which subsequently was accepted by the Board. The court found that the June 26 offer expired at noon on June 27, because the language in defendant's June 20 letter provided that "any other alternative" would expire on that day.<sup>8</sup> If the court had confined itself to the issues argued in the parties' briefs, this finding would have mandated affirmance of the verdict and judgment of the lower court.

Plaintiff's letters constituted a counter-offer. If an offer contains an express provision limiting the time for acceptance the provision must be complied with, or the offer will lapse when the deadline passes.<sup>9</sup> If the offeree thereafter attempts to accept the offer, this purported acceptance will not form a contract. A late acceptance, however, is effective as a counter-offer, which, if accepted by the original offeror, will create a contract.<sup>10</sup> The court clearly was correct in finding that plaintiff's June 30 letters were

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4. 268 S.C. at 586, 235 S.E.2d at 293. The venerable rule is that a party is entitled to a directed verdict if only one inference may be reasonably drawn from the facts. *Dunsil v. E.M. Jones Chevrolet Co., Inc.*, 268 S.C. 291, 233 S.E.2d 101 (1977); *Kirkland v. Hardwicke Chem. Co.*, 262 S.C. 520, 205 S.E.2d 831 (1974). This standard is made even more stringent by requiring the trial court to consider the testimony in the light most favorable to the party resisting the motion. *Farr v. Duke Power Co.*, 265 S.C. 356, 218 S.E.2d 431 (1975); *Hart v. Doe*, 261 S.C. 116, 198 S.E.2d 526 (1973). It is therefore unusual for an appellate court to overturn a jury verdict on the grounds that a verdict should have been directed for the appellant.

5. "As the offeror is at liberty to make no offer at all he is also at liberty to dictate whatever terms he sees fit if he chooses to make an offer." 1 S. WILLISTON, *CONTRACTS* § 53 (3d ed. 1957).

6. Brief for Respondents at 4.

7. Brief for Appellant at 6 (citing 1 A. CORBIN, *CONTRACTS* § 36 (1963)).

8. 268 S.C. at 587, 235 S.E.2d at 293.

9. A. CORBIN, *CONTRACTS* § 35 (1963); 1 S. WILLISTON, *CONTRACTS* § 53 (3d ed. 1957); *RESTATEMENT (SECOND) OF CONTRACTS* § 40 (Tent. Drafts Nos. 1-7, 1973).

10. *RESTATEMENT (SECOND) OF CONTRACTS* § 73 (Tent. Drafts Nos. 1-7, 1973).

a counter-offer.

The court held, however, that the Board accepted this counter-offer:

Appellant's resignation was tendered premised on the continuation of his salary through December, the identical terms of the Board's lapsed offer. The Board's written acceptance of the resignation expressed a consent to be bound by the terms of the resignation and formed a binding contract between the parties. *Unqualified acceptance* of the resignation bound the Board to the terms of the resignation.<sup>11</sup>

In two respects, this holding is contrary to general contract law and to the facts as stated by the court. First, the court apparently overlooked a basic premise of contract law: for a contract to exist, mutual assent must be present. The common statement of this principle is that a "meeting of the minds" of the parties must occur.<sup>12</sup> There is a serious question whether the minds of Cain and the Board did meet. As the court recognized, plaintiff's resignation was tendered conditionally and could be accepted only if the Board agreed to his salary proposal. During the telephone conversation of June 30, the Board communicated to plaintiff a purported acceptance that undoubtedly varied the terms of the offer. Refusing to pay plaintiff's salary rendered the acceptance ineffectual, and the Board could rightly argue that no contract came into existence.<sup>13</sup>

Second, the court opined that the written acceptance of the resignation embodied in the July 8 letter from defendants to plaintiff, expressed an "unqualified" consent to be bound. That communication expressly referred to the conversation of June 30, wherein plaintiff was informed that the Board would not pay his salary. The court was therefore misguided in characterizing the acceptance as "unqualified."<sup>14</sup>

11. 268 S.C. at 587, 235 S.E.2d at 293-94 (emphasis added) (citations omitted).

12. *Kitchens v. Lee*, 221 S.C. 59, 66, 69 S.E.2d 67, 69 (1952); *Stein v. Xepapas*, 204 S.C. 239, 246, 29 S.E.2d 257, 259 (1944).

13. See RESTATEMENT (SECOND) OF CONTRACTS § 60 (Tent. Drafts Nos. 1-7 1973): "A reply to an offer which purports to accept it but is conditional on the offeror's assent to terms additional to or different from those offered is not an acceptance but is a counter-offer." The Board's purported acceptance cannot be construed as merely requesting a change in the terms of the offer, because the Board obviously would not bind itself to pay plaintiff's salary and then naively ask that he agree not to accept it. See *id.* § 62.

14. Arguably, the court should have considered the telephone conversation and not the subsequent letter in determining whether a contract was formed. Because plaintiff's offer did not require the Board's written acceptance, the Board could accept in any reasonable manner. See *id.* § 29. A telephone call is arguably a reasonable manner of

A possible basis for the court to decide in plaintiff's favor, if moved by the equities to do so, was presented by plaintiff's argument that for the time limit to be effective it had to be relayed with sufficient definiteness.<sup>15</sup> Because the court was constrained to view the evidence in the light least favorable to plaintiff,<sup>16</sup> however, such a decision would undoubtedly have been unjustified. The supreme court was correct in resolving for defendant the deadline issue briefed and argued. It was correct in holding that plaintiff's purported acceptance of defendant's offer was a counter-offer. Nevertheless, in an apparent attempt to avoid a result it considered inequitable, the court erred in holding defendant unconditionally accepted the counter-offer. While the final disposition of this case should not offend anyone's sense of fairness, the court's function is not to twist established rules of law to reach a desired result. This practice can lead only to an unacceptable degree of uncertainty in the law.

## II. THE UNIFORM COMMERCIAL CODE AND COMMON-LAW CONTRACT PRINCIPLES

The most important development in contract law in this century was adoption of Article Two of the Uniform Commercial Code (UCC) which deals with sales of goods. Much of Article Two simply codifies preexisting contract law,<sup>17</sup> though some provisions were novel when introduced.<sup>18</sup> Parties will try to bring a case under the umbrella of Article Two to take advantage of favorable sections. At times, however, the common law and the UCC will lead to the same result.

In *Ranger Construction Co. v. Dixie Floor Co.*,<sup>19</sup> the United States District Court for the District of South Carolina had to

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acceptance; therefore, the subsequent letter should be considered a mere confirmation of the contract and not an acceptance itself.

15. See note 7 and accompanying text *supra*.

16. Plaintiff's ground for appeal was the trial judge's failure to grant his motion for a directed verdict. See note 4 *supra*.

17. Professor Gilmore, speaking of the Code in its entirety, stated:

It derives from the common law, not the civil law, tradition. We shall do better to think of it as a big statute—or a collection of statutes bound together in the same book—which goes as far as it goes and no further. It assumes the continuing existence of a large body of pre-Code and non-Code law on which it rests for support, which it displaces to the least possible extent, and without which it could not survive.

Gilmore, *Article 9: What It Does for the Past*, 26 LA. L. REV. 285, 285-86 (1966).

18. See, e.g., U.C.C. §§ 2-312 to -318.

19. 433 F. Supp. 442 (D.S.C. 1977).

decide whether the contract before it was governed by the Code or by common-law principles. Defendant, a subcontractor, contracted with plaintiff, a general contractor, to "furnish all materials and labor for the installation of resilient flooring in the Clinical Science Building at the Medical University of South Carolina at Charleston." Defendant refused to perform and plaintiff had to contract with another flooring dealer to perform the work at a price allegedly \$22,268 above that specified in the original contract. Plaintiff filed suit for that amount.

Defendant admitted the validity of the contract, but claimed its performance was excused because of circumstances that had arisen during prior dealings with plaintiff. The parties had entered into a similar contract just prior to signing the contract in question. Under the prior contract defendant fully performed, but plaintiff for no valid reason, refused to pay the amount due. Defendant reduced its claim to judgment before plaintiff paid anything. Payment for the prior contract was finally received, but not until after plaintiff requested, and defendant refused, to begin work at the Medical University site.

On plaintiff's motion for summary judgment, defendant used the prior contract as justification for its actions and based its argument on two legal theories. First, the transaction was subject to the provisions of Article Two of the UCC,<sup>20</sup> and under section 2-609 defendant was excused from performance. Second, the common law as embodied in section 280 of the First Restatement of Contracts excused its refusal to perform. The court denied plaintiff's motion holding that a question of fact was raised under the second theory.<sup>21</sup> The court's disposition of these two arguments is considered separately below.

#### *A. The Applicability of Article Two of the Uniform Commercial Code*

Defendant's primary argument was that there was an issue of fact over whether Ranger's breach of the prior contract constituted "reasonable grounds for insecurity" under UCC section 2-609.<sup>22</sup> That section permits a contracting party who has reasonable grounds for insecurity to suspend performance, demand assurance from the other party, and, if assurance is not forthcoming

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20. S.C. CODE ANN. §§ 36-2-101 to -809 (1976).

21. 433 F. Supp. 442 (D.S.C. 1977).

22. 433 F. Supp. at 443-44.

ing, treat the contract as repudiated.<sup>23</sup> Plaintiff contended that Article Two of the UCC did not apply to the transaction, because the scope of Article Two as defined in section 2-102, applies only to “transactions in goods.”<sup>24</sup>

Defendant argued that under its contract with plaintiff it was required to furnish the flooring materials for the building and that these materials were questionably “goods” as defined in the Code.<sup>25</sup>

When goods are involved in a transaction, however, they do not necessarily transform it into a “transaction in goods.”<sup>26</sup> If a contract involving both services and materials is predominantly one for rendering services, courts will not apply Article Two to determine the rights and obligations of the parties.<sup>27</sup> The court in *Ranger*, quoting from *Bonebrake v. Cox*,<sup>28</sup> applied the following test:

“The test for inclusion or exclusion [of contracts for goods and services] is not whether they are mixed, but, granting that they are mixed, whether their predominant factor, their thrust, their purpose, reasonably stated, is the rendition of service with goods incidentally involved (*e.g.*, contract with artists for painting) or

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23. S.C. CODE ANN. § 36-2-609 (1976) provides:

**Right to Adequate Assurance of Performance.**

(1) A contract for sale imposes an obligation on each party that the other's expectation of receiving due performance will not be impaired. When reasonable grounds for insecurity arise with respect to the performance of either party the other may in writing demand adequate assurance of due performance and until he receives such assurance may if commercially reasonable suspend any performance for which he has not already received the agreed return.

(2) Between merchants the reasonableness of grounds for insecurity and the adequacy of any assurance offered shall be determined according to commercial standards. . . .

(4) After receipt of a justified demand failure to provide within a reasonable time not exceeding thirty days such assurance of due performance as is adequate under the circumstances of the particular case is a repudiation of the contract.

24. U.C.C. § 2-102.

25. 433 F. Supp. at 444. *See* U.C.C. § 2-105(1), which defines goods as: all things (including specially manufactured goods) which are movable at the time of identification to the contract for sale other than the money in which the price is to be paid, investment securities (Article 8) and things in action. “Goods” also includes the unborn young of animals and growing crops and other identified things attached to realty as described in the section on goods to be severed from realty (Section 2-107).

26. R. NORDSTROM, LAW OF SALES § 22 (1970).

27. *Id.*

28. *Bonebrake v. Cox*, 499 F.2d 951 (8th Cir. 1974).

is a transaction of sale, with labor incidentally involved (e.g., installation of a water heater in a bathroom).<sup>29</sup>

Nothing is really profound about the *Bonebrake* formulation. It simply requires a court to examine each case to determine whether the sale or the service factor carries the greater weight. In *Ranger*, the court found that the service element prevailed. The court looked to the terms of the contract, wherein defendant was referred to as a subcontractor, not as a materialman, and the answers to interrogatories, which indicated that defendant's business was not that of a wholesaler of flooring materials, but of an installer of the materials. Furthermore, the determination that the service element dominated was clearly supported by the record.

*B. Section 280 of the Restatement (First) of Contracts as a Common-Law Substitute for Section 2-609 of the Uniform Commercial Code*

Defendant also alleged a common-law defense to the breach of contract action. Plaintiff argued in its brief that "the breach of another and separate contract cannot be pled as a defense in a contract action."<sup>30</sup> Defendant argued, however, that plaintiff's wrongful failure to pay under the prior contract indicated plaintiff's prospective unwillingness or inability to pay for performance under the contract in issue, so that defendant was excused from performance or was entitled to receive assurance of performance from plaintiff.<sup>31</sup> This position was based upon the principle of prospective failure of consideration stated in section 280 of the *Restatement (First) of Contracts*:<sup>32</sup>

*Manifestation by One Party of Inability to Perform or of Intention Not to Perform*

(1) Where there are promises for an agreed exchange, if one promisor manifests to the other that he cannot or will not substantially perform his promise, or that, though able to do so, he doubts whether he will substantially perform it, and the statement is not conditional on the existence of facts that would justify a failure to perform, and there are no such facts, the other

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29. 433 F. Supp. at 444, (quoting 499 F.2d 951, 960 (8th Cir. 1974)).

30. 433 F. Supp. at 445. See *Hal Roach Studios v. Film Classics*, 156 F.2d 596 (2d Cir. 1946); *Hanson & Parker v. Wittenberg*, 205 Mass. 319, 91 N.E. 383 (1910); *Northwest Lumber Sales, Inc. v. Continental Forest Prod.*, 261 Or. 480, 495 P.2d 744 (1972).

31. 433 F. Supp. at 446.

32. RESTATEMENT (FIRST) OF CONTRACTS § 280 (1932).



party is justified in changing his position, and if he makes a material change of position he is discharged from the duty of performing his promise.

(2) The party making a statement within the rule stated in Subsection (1) has power to nullify the effect of the statement by a retraction, as long as the other party has not materially changed his position.<sup>33</sup>

The court, while pointing out that no South Carolina law is available on this point, found that courts in other jurisdictions agree with the law as set out in the *Restatement*.<sup>34</sup> The court refused to grant summary judgment for Ranger because under section 280 a “question of fact for the jury existed whether plaintiff’s refusal to pay defendant under their [prior contract] constituted a manifestation to the defendant that plaintiff could not or would not substantially perform his promise under the contract.”<sup>35</sup>

The rationale behind the doctrine of prospective failure of consideration is that although a party to a contract assumes the risk that the other party will perform, performance should not be required when it clearly will result only in a right to sue the other party.<sup>36</sup> Parties to a contract bargain for each other’s performances, not for a lawsuit. Although the *Restatement* is not mentioned, the comments to section 2-609 of the Uniform Commercial Code demonstrate that the provision is a lineal descendant of the doctrine of prospective failure of consideration.<sup>37</sup> While Dixie was unable to utilize the Code provision directly because of the nature

33. *Id.*

34. 433 F. Supp. at 446. The court cited *New York Life Ins. Co. v. Viglas*, 297 U.S. 672 (1936), and *Kimel v. Missouri Life Ins. Co.*, 71 F.2d 921 (10th Cir. 1934).

35. 433 F. Supp. at 446.

36. RESTATEMENT (FIRST) OF CONTRACTS § 280, Comment a (1932).

37. See U.C.C. § 2-609, comment 1:

The section rests on the recognition of the fact that the essential purpose of a contract between commercial men is actual performance and they do not bargain merely for a promise, or for a promise plus the right to win a lawsuit and that a continuing sense of reliance and security that the promised performance will be forthcoming when due, is an important feature of the bargain. If either the willingness or the ability of a party to perform declines materially between the time of contracting and the time for performance, the other party is threatened with the loss of a substantial part of what he bargained for. . . .

*Id.*

of the contract, it did succeed in having the court apply the common-law rule from which the provision was derived.<sup>38</sup>

*Walter W. Theus, Jr.*

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38. RESTATEMENT (SECOND) OF CONTRACTS § 275 (Tent. Draft No. 9, 1974) was designed to replace section 280 of the First *Restatement*. It reads:

§ 275. When a Failure to Give Assurance May be Treated as a Repudiation

(1) Where reasonable grounds arise to believe that the obligor will commit a breach that would of itself give the obligee a claim for damages under § 268, the obligee may demand adequate assurance of due performance and may, if reasonable, suspend any performance for which he has not already received the agreed exchange until he receives such assurance.

(2) The obligee may treat the obligor's failure to provide within a reasonable time such assurance of performance as is adequate in the circumstances of the particular case as a repudiation.

The comments and reporter's notes to this section cite the UCC provision as its primary source. The section demonstrates the manner in which the draftsmen of the Second Restatement have sought to harmonize the law on nonsales transactions with that set forth in the UCC.