

CONTRACTS
Professor John Orcutt
Fall Semester 2005

MIDTERM EXAMINATION – IN CLASS

INSTRUCTIONS:

1. This is a closed-book examination. You may not bring any materials to the examination with the exception of ESL students who are allowed to bring and use a Home Language/English dictionary.
2. This is a 1-hour examination and is worth 60 points. The examination consists of:
 - ▶ 7 multiple choice questions that will be worth 2 points each (for a total of 14 points)
 - ▶ 2 Essay Questions: Question No.1 will be worth 34 points and Question No. 2 will be worth 12 points.

It is your responsibility to apportion your time appropriately amongst the questions. If you base your time on the possible points per question, the time apportionment should be:

- ▶ Multiple choice questions = 2 minutes per question (for a total of 14 minutes)
 - ▶ Essay Questions = 10 minutes to read and consider the hypothetical and:
 - 26 minutes to write your answer for Essay Question No. 1
 - 10 minutes to write your answer for Essay Question No. 2
3. The grading of examinations is anonymous. So, you must write your examination number on the examination, your blue book and your Scantron sheet. **YOU MAY NOT WRITE YOUR NAME ON ANYTHING – YOU MAY ONLY USE YOUR EXAM NUMBER.**
 4. ***For the multiple choice questions:*** The multiple choice questions are to be answered on a Scantron sheet. Your proctor will provide you with specific instructions regarding the filling out of the Scantron sheet.
 5. ***For the essay questions:*** Please write your answers in a blue book. Remember to write your examination number on your blue book. The only answers that will be graded are the answers written into a blue book. While you are free to use scratch paper, answers written on scratch paper, or anything else other than a blue book, will not be read and will not be counted for any credit. Please write only on the front side of the pages in the blue book. Please remember that organization, persuasiveness, neatness and legibility all count in determining your grade on the essay answers. To improve the organization of an answer, you may wish to quickly outline the answer on a separate sheet of paper prior to writing your full answer in the blue book.
 6. I have tried my best to write and proofread the exam so that there are no distracting typos or other errors – but, I may not have been totally successful. If you believe there is a typo or other error that makes it difficult to answer a particular question, make your best selection and write out the error on the back of the Scantron sheet (for the multiple choice questions) or in your blue book (for the essay questions) and any assumption you used to answer the question. Be sure to indicate the number of the question involved.

Good luck on the examination!

DO NOT TURN TO PAGE 2 UNTIL THE PROCTOR TELLS YOU TO BEGIN

MULTIPLE CHOICE QUESTIONS

(2 points each)

Question No. 1

Danny Way is looking to raise a little money and has decided to sell a skateboard from his collection of classic skateboards. Danny placed the following advertisement in the local newspaper:

FOR SALE. Classic 1978 Wes Humpston Big Foot Model Skateboard. Vintage condition. \$450 firm. First caller gets it. Call Danny at 228-1541.

Brian Sommese, an avid skateboarder, sees the advertisement in the newspaper and immediately calls Danny at which point the following exchange occurs:

Danny: "Hello."

Brian: "I accept your offer for the Wes Humpston Big Foot Model Skateboard."

Danny: "Sorry, I've changed my mind. I've decided not to sell it."

Brian: "You can't do that. We have a deal. You have to sell me that skateboard."

What is the most correct statement regarding Brian's claim that he has entered into a contract with Danny?

- (A) There was no contract formed because advertisements are not offers.
- (B) There was no contract formed because advertisements are generally not offers
- (C) A contract probably was formed because this advertisement was an offer.
- (D) There was no contract formed because if the advertisement was an offer, Danny rescinded the offer.

Questions No. 2

Fidelity Telecom Inc. ("Fidelity") Fidelity is a full-service competitive telecom services provider that services the business community. One of Fidelity's clients is Wu Tang Financial LLP ("Wu Tang Financial"), one of the leading wealth management companies on Wall Street. In 1999, Fidelity entered into a 10-year Communication Services Agreement (the "1999 Communication Services Agreement") with Wu Tang Financial at the then prevailing rates for such services. Since 1999, the price for communication services has dropped steadily. Apparently, Wu Tang Financial is not happy with the rates it was paying under the 1999 Communications Services Agreement and has contacted Fidelity.

Dirt McGirt, the CEO of Wu Tang Financial, called up Martha Stewart, the CEO of Fidelity. At that time, Dirt expressed his dissatisfaction with the rates charged under the 1999 Communication Services Agreement. Specifically, Dirt threatened to cancel the agreement if Wu Tang Financial did not receive a 50% reduction in the rates. Martha responded by sending Dirt an official amendment letter (the "Amendment Letter"). The text of the Amendment Letter was as follows:

"For good and valuable consideration, the sufficiency of which is hereby acknowledged, Wu Tang Financial LLP and Fidelity Telecom Inc. hereby mutually agree that the rates currently specified in the 1999 Communications Services Agreement shall be reduced by 40%."

Wu Tang's obligations to Fidelity did not change in any matter under the Amendment Letter.

Both Dirt and Martha signed the Amendment Letter. A few days after entering into the Amendment Letter, Fidelity decided that it no longer wished to provide Wu Tang with such a substantial rate reduction and informed Dirt. Wu Tang has sued Fidelity to compel Fidelity to honor its commitment in the Amendment Letter to reduce Wu Tang's rates by 40%.

What is the most accurate statement regarding the potential outcome of the dispute?

- (A) There was adequate consideration to bind Fidelity's promise to reduce Wu Tang's rates.
- (B) If the court applies the pre-existing duty rule, Fidelity's promise to reduce Wu Tang's rates will likely be deemed unenforceable.
- (C) If the court applies the pre-existing duty rule, Fidelity's promise to reduce Wu Tang's rates will likely be deemed enforceable.
- (D) Because the Amendment Letter was signed by both parties, the Amendment Letter is enforceable.

Question No. 3

Acme Corp. (“Acme”) is a leading provider of data security services. Acme finds and solves security problems in a client’s computer systems. Acme’s largest competitor is Beta, Inc. (“Beta”), which provides largely the same service to the same general class of clients as Acme.

Acme received information that Beta had been hacking into Acme’s computer systems and gaining access to highly sensitive information from Acme. At first, Acme considered both pressing criminal charges and bringing a civil lawsuit against Beta. Acme, however, was very concerned about the negative press from such legal actions (how would it look if Acme cannot protect its own computers systems?). Instead, Acme decided to fix the problem more quietly. First, Acme found the weakness in its computer security system and fixed it. Second, Acme decided that it had to retrieve its confidential information from Beta. To conduct this retrieval, Acme decided to hire Jack Bauer, who is a former CIA agent who now works on highly sensitive projects for companies. Specifically, Acme entered into an agreement with Jack (the “Consulting Agreement”) whereby Acme agreed to pay Jack \$500,000 in exchange for Jack’s promise to break into Beta’s headquarters and locate and retrieve the missing files. Acme believed the missing files were all located in a special server that was kept in a high security vault within Beta. Jack was to obtain, and bring back to Acme, this special server. Acme paid the \$500,000 immediately following execution of the Consulting Agreement. After entering into the Consulting Agreement, Jack decided not to go through with the assignment and so informed Acme. Acme asked Jack to return the \$500,000, but Jack refused.

Acme is considering filing a lawsuit against Jack to force him to return the \$500,000. What is the most accurate statement regarding the potential outcome of Acme’s lawsuit:

- (A) The Consulting Agreement is a bilateral contract. As such, Acme is entitled to recover the \$500,000 because Jack has not performed his promise, which was bound by Acme’s promise.
- (B) The Consulting Agreement is void as an illegal contract. As such, Jack must return the \$500,000 to Acme.
- (C) The Consulting Agreement is void as an illegal contract. As such, Acme is not entitled to recover the \$500,000.
- (D) The Consulting Agreement is a unilateral contract. Since Jack has not fully performed, Jack must return the \$500,000 to Acme.

Question No. 4

A Corp. entered into a lease agreement (the "Lease Agreement") with Z Corp. whereby A Corp. leased a warehouse facility in Xanadu from Z Corp. for a 10-year term (the "Term"). At the time of contracting, A Corp. wanted to have the ability to extend the lease upon the expiration of the Term. As a result, A Corp. and Z Corp. included the following renewal clause in the Lease Agreement:

Renewal Clause: Beginning 3 months before the expiration of the term of this lease and running until the expiration of this lease, Lessee shall have the right to renew this lease for an additional five years at the "Renewal Rent Rate". The Renewal Rent Rate shall be calculated as the then market rate for similar warehouse space in the warehouse district of Xanadu. Lessee and Lessor hereby agree to act in good faith in determining the Renewal Rent Rate. In the event that the parties are unable to agree on the Renewal Rent Rate, the Renewal Rent Rate shall be determined by binding arbitration. Lessee and Lessor further specify that \$100 per month of the current Rental Rate shall be attributable as Lessee's payment for this renewal option."

Three months before the expiration of the Lease Agreement, A Corp. exercised its right to renew the lease. After a few weeks of negotiation, A Corp. and Z Corp. were having trouble reaching agreement on the Renewal Rent Rate. A Corp. decided that it no longer wished to renew the Lease Agreement and so informed Z Corp. Z Corp. responded by stating that A Corp. had to renew the Lease Agreement and filed a law suit.

What is the most correct statement regarding the potential outcome of Z Corp.'s lawsuit?

- (A) A Corp. should prevail because the renewal clause is fatally indefinite
- (B) Z Corp. should prevail because A Corp.'s exercise of the renewal clause included an implied option contract which was bound by promissory estoppel.
- (C) A Corp. should prevail because there was no meeting of the minds between A Corp. and Z Corp.
- (D) Z Corp. should prevail because A Corp. formed a contract with Z Corp. regarding the renewal clause and A Corp.'s revocation was therefore too late.

Question No. 5

Paul and Diane are long-time friends and joint owners of a parcel of land (the "Parcel"). Paul owns 60% of the Parcel and Diane owns 40%. On July 1st, Diane informed Paul that she was thinking about selling her 40% interest and asked if he was interested in buying it. Paul said that he was if the price was right. On July 8th, Diane sent Paul the following letter:

"Paul,

I agree to sell you my 40% interest in the Parcel for \$200,000 in cash.

Very truly yours,

/s/ Diane"

Paul received the letter on July 9th. Paul was interested in the proposal, but unfortunately did not have enough funds on hand to complete the transaction. To raise the funds, Paul sold a house that he owned (the "House Sale"). The House Sale was completed on August 15th, at which time Paul had roughly \$500,000 in his bank account. On August 21st, Paul sent the following letter to Diane:

"Diane,

I accept your proposal dated July 8th. I have enclosed a check for \$25,000 as a down payment. I have made arrangements to get you the rest.

Sincerely,

/s/ Paul"

After receiving Paul's letter, Diane called Paul to tell him that she was no longer interested in selling her 40% interest in the Parcel. Paul filed suit against Diane.

Which of the following statements reflects an "improper" application of law by the court in trying to resolve the case?

- (A) If Diane's letter is deemed to be an offer for a bilateral contract, the mirror image rule could be deemed satisfied.
- (B) Diane's offer may have lapsed.
- (C) If Diane's letter is deemed an offer for a bilateral contract and the offer had not yet lapsed, Paul's acceptance was invalid because Diane retracted the offer.
- (D) If Diane's letter is deemed an offer for a unilateral contract, Paul may be viewed as having commenced performance, which restricted Diane's ability to retract the offer.

Question No. 6

Johnny O. is a Contracts professor at a law school in New England. During his review session for the midterm examination, which took place one week prior to the exam, Johnny O. made the following announcement to the class:

“I have been teaching Contracts for a few years, and I find that providing students with concrete goals and rewards does wonders for their performance. So, I am offering \$500 to the student that receives the highest grade on the midterm examination. I understand that you have a lot of commitments to balance, including a memo for your skills course, but I want to give you some motivation to spend more time focusing on my exam.”

The Dean of the Law School learned of Johnny O.’s proposal and told Johnny O. that he did not want Johnny O. to follow through on the announcement. The Dean explained that Paragraph 23(a)(3)(iv) of the Faculty Code Book provides that “professors may not pay students for classroom performance.” Just prior to the exam, Johnny O. announced to the class that he would not be able to provide the \$500 for the highest score as previously promised.

Neva Gonagettit, a student in Johnny O.’s class, received the highest grade on the midterm exam. She worked very hard to prepare for the exam (including having foregone a number of social events) and feels entitled to the \$500. Neva has threatened to file suit against Johnny O. What is the most correct statement regarding her potential suit?

- (A) Neva should not prevail because the agreement violates the law.
- (B) Neva should prevail if Neva’s preparation for the exam prior to Johnny O.’s retraction is deemed to be partial performance.
- (C) Neva should not prevail because the offeror is the master of the offer and has an absolute right to revoke the offer.
- (D) Neva should prevail because although the agreement violates the law, Neva was justifiably unaware of the illegality.

Question No. 7

As we all know by now, Ashley Simpson is one of the most talented singers in America (if not the world). Unfortunately, while Ashley has a voice that can only be described as divine, her throat muscles (which are key to singing) are actually quite weak. These weak throat muscles have caused Ashley to cancel a number of concert engagements in the past because, on occasion, her throat muscles simply were not strong enough to allow her to sing at the high level that her fans expect from her.

Two years ago, Ashley entered into a contract with NKOTB Concerts (the “Concert Contract”) to conduct a nationwide concert tour. Because of Ashley’s throat condition, Ashley agreed to below market-rate compensation for her agreement to conduct concerts. Under the Concert Contract, Ashley agreed to perform 100 concerts in 2004 for \$5 million and 100 concerts in 2005 for \$6 million. During 2004, Ashley realized that her

weak throat was caused by smoking and drinking too much coffee. Ashley gave up both vices in 2004. Her throat muscles strengthened and Ashley did not miss a single performance in 2004. At the beginning of 2005, Ashley informed Jordan Knight, the CEO of NKOTB Concerts, that she wanted more money for the 2005 concert season. Eventually, Jordan provided Ashley with the following hand-written letter (the "Bonus Letter"):

"NKOTB Concerts agrees that should Ashley Simpson draw more than 2,000,000 patrons to her concerts during 2005, NKOTB Concerts will pay Ashley a \$2 million bonus.

/s/ Jordan Knight"

As of September 15, 2005, Ashley had performed in 70 concerts and attracted over 1.8 million fans. On September 16, 2005, Jordan Knight informed Ashley that he was rescinding the Bonus Letter. Ashley has sued NKOTB Concerts to collect the \$2 million bonus from the Bonus Letter. What is the most accurate statement regarding the potential outcome of Ashley's lawsuit?

- (A) Ashley will likely win because NKOTB Concerts was not entitled to revoke its offer under the Bonus Letter due to Ashley's performance.
- (B) Ashley will likely lose because under the pre-existing duty rule there was no consideration to support NKOTB Concerts' promise to pay \$2 million under the Bonus Letter.
- (C) Ashley will likely win. The Bonus Letter is an offer for a unilateral contract. As a result, Ashley's commencement of performance is sufficient to form a binding unilateral contract.
- (D) Ashley will likely lose because she did not counter-sign the Bonus Letter. As a result, she did not accept NKOTB Concerts' offer and NKOTB Concerts was free to revoke the offer.

SCUDDER & ROBICHEAUX

Attorneys at Law

Memorandum

Re: Build It and They Will Come

September 27, 2005

To: Alex Associate
From: Mary Russell Holmes

I am glad that you are available to help on this matter. It is rather complicated so I want to put together my best team to work on the problem. As you probably know, ABC Inc. ("ABC") is one of the firm's bigger clients. ABC is a general contracting firm that specializes in large commercial real estate development projects. In plain English, ABC builds large office buildings and commercial real estate parks.

Recently, ABC bid on a large construction project to build a 32-story office building. The general contractor bids for the project were due by 1:00 p.m. on July 26th. As part of the process for calculating its general contractor bid, ABC solicited bids from a number of different subcontractors, including five different roofing subcontractors. The five roofing subcontractors were asked to submit a bid by 1:00 p.m. on July 25th for installing a roof on the office building. The five roofing subcontractors submitted the following bids:

- Subcontractor 1 = \$17.2 million
- Subcontractor 2 = \$14.0 million
- Subcontractor 3 = \$17.0 million
- Subcontractor 4 = \$17.5 million
- Subcontractor 5 = \$17.2 million

At first glance, ABC was surprised at how low Subcontractor 2's bid was compared to the other roofing subcontractors. In the end, ABC figured that Subcontractor 2 must have known what it was doing and decided to use Subcontractor 2's bid for purposes of calculating its general contractor bid. Subcontractor 2's bid contained no language regarding the duration of its effectiveness.

On August 1st, ABC was awarded the contract. ABC has often used Subcontractors 1 and 3 on high-rise projects. Over the next week, ABC contacted each of Subcontractors 1 and 3 to see if they could match Subcontractor 2's bid and do the project for \$14.0 million. Both Subcontractors 1 and 3 said they could not lower their bids. On September 23rd, after much deliberation, ABC had decided that it was going to accept Subcontractor 2's offer. As ABC was preparing to call Subcontractor 2 with the good news, Subcontractor 2 called ABC to inform ABC that its \$14.0 million bid was mistaken and was withdrawn. ABC informed Subcontractor 2 that withdrawing the bid was unacceptable and that ABC considered itself to have a binding contract with Subcontractor 2.

Your Assignment

This is where we come in. ABC would like for us to examine whether it can hold Subcontractor 2 to its bid. Please analyze ABC's contractual rights vis-à-vis Subcontractor 2. The question seems simple to me: Subcontractor 2 has promised to build a roof for \$14.0 million. I understand, however, that the analysis may be a little more complicated. I think there are two primary approaches that courts' take in examining the revocability/enforceability of subcontractor bids.

Specifically, this is what I need from you:

Question No. 1 (34 points possible):

- (a) Provide a breakdown/diagram of the various steps in the subcontractor bidding process and explain what each steps represents in the formation of a contract (e.g., offer, acceptance, etc.).
- (b) Please examine whether Subcontractor 2 can be legally required to honor its \$14.0 million bid. In conducting your analysis please consider each of the two primary approaches employed by courts.

Question No. 2 (12 points possible):

One last quick, but related issue. ABC also sought subcontractor bids for the plumbing work to be done on the project. In formulating its general bid, ABC used the bid submitted by Drano Inc. ("Drano"). While ABC used Drano's bid in formulating the general bid, ABC does not want to use Drano on the actual project. ABC would prefer working with Tidy-Bowl Co., a company with whom ABC has worked on numerous occasions. Is ABC required to use Drano on the project? Please explain.

- END OF EXAM -