

ESSAY QUESTION NO. 7

Answer this question in booklet No. 7

Maude lives in Stormy, Alaska, located near the end of the Aleutian Island chain. Stormy's climate is moderate, but it is subject to high winds and frequent cyclonic storms. StormyAir provides the only passenger jet service to Anchorage two days per week, weather permitting.

Maude works for the City of Stormy ("City") as the chief mechanic for the City's small boat fleet. The City came to believe that Maude was stealing tools from the City for use by Buoy Boats, a business Maude was running on the side.

On April 26, the City fired Maude from her job. The next morning, the City filed a civil suit against Maude alleging that she had converted City tools and equipment to her own use. Damages were alleged to be in excess of \$20,000. The City also obtained an ex parte writ of attachment of Maude's accounts, monies, possessions, property, assets and wages. The writ was validly issued and served that day. The City police officers serving the writ seized Maude's tools and informed Maude that anything she purchased, such as a plane ticket, would be subject to execution. Maude contends that the seizure of her tools left her unable to operate Buoy Boats.

Later in the day, Maude received a phone call from her sister, telling her that their mother was gravely ill and rapidly deteriorating, and that Maude should come to the Anchorage Hospital right away.

Maude immediately went to the StormyAir ticketing counter at the airport, where a ticketing agent informed Maude that she could not let her on a plane without permission from Calvin, the City's attorney. Calvin had discussed the writ with the StormyAir ticketing agent, but claims he told the agent that the City had no intent to seize any airline tickets or otherwise prevent Maude from coming to or going from Stormy of her own free will.

Maude left the airport, went directly to Calvin's office, and insisted that everything be settled so that she could leave Stormy.

Calvin proposed the following settlement terms: Maude would confess judgment in favor of the City in the sum of \$10,000 and would transfer her interest in the seized tools to the City. The tools were valued in the settlement at \$15,000. Maude would agree to forever release and settle any and all claims she may have against the City, and would pay the City's attorney's fees if she breached the agreement.

The settlement also contained a "liquidated damages" clause providing that "should Maude breach any part of this agreement, the sum of \$10,000 will be

forfeited to the City of Stormy as liquidated damages for the breach and the City will be free to press the claims settled herein.” In exchange, the City agreed to settle the claims asserted in its complaint.

Maude signed the agreement, borrowed money from friends in order to purchase a plane ticket, and took the first flight to Anchorage.

1. Maude claims that she executed the settlement agreement under duress and seeks to have the agreement voided. Discuss the merits of Maude’s duress claim.
2. Is the liquidated damages clause in the settlement agreement valid? Discuss.

GRADER'S GUIDE

*** QUESTION NO. 7 ***

SUBJECT: CONTRACTS

1. Maude claims that she executed the agreement under duress and seeks to have the agreement voided. Discuss the merits of Maude's duress claim. (60 points)

Maude and the City entered into a settlement agreement in which Maude would pay the City \$10,000, transfer ownership of roughly \$15,000 worth of tools and equipment to the City, and release any claims she might have against the City. The City agreed to settle the claims asserted in its complaint. Maude now claims that she signed the agreement under duress.

If a contract sought to be avoided is the settlement of litigation, Alaska courts will consider "the manner in which the release was obtained, including whether it was hastily secured at the instigation of the releasee, whether the releasor was represented by counsel, and whether [the releasor] relied on the representations of the releasee. Finally, the relative bargaining positions of the parties should be weighed." *Schmidt v. Lashley*, 627 P.2d 201, 204 (Alaska 1981) (citing *Witt v. Watkins*, 579 P.2d 1065, 1070 (Alaska 1978)). The considerations outlined in *Schmidt* were applied in *Helstrom v. North Slope Borough*, 797 P.2d 1192, 1198 (Alaska 1990), a case in which one party to a mutual release sought to void the release on the grounds of duress. There, the court regarded the party challenging the release as the "releasor" when discussing the *Schmidt* considerations, although technically both parties had released one another from claims.

The Alaska Supreme Court first addressed the claim of duress in *Totem Marine Tug & Barge, Inc. v. Alyeska Pipeline Serv. Co.*, 584 P.2d 15 (Alaska 1978). In order to void a contract on the basis of duress, three elements must be proven: (1) one party involuntarily accepted the terms of another, (2) circumstances permitted no other alternative, and (3) such circumstances were the result of coercive acts of the other party. *Id.* at 21.

a. Involuntariness prong

The involuntariness prong of the test is subjective. The question is not whether a reasonable person's will would have been overcome, but rather whether the will of the party asserting the duress claim was overcome by the opposing party's actions. *Helstrom v. North Slope Borough*, 797 P.2d 1192, 1198 (Alaska 1990). Maude's simple assertion that she signed the agreement involuntarily is enough to satisfy the first requirement. *Id.* Maude would probably maintain that because she had no continuing means of financial

support in Stormy and believed that she was unable to leave the island without settling with the City, she subjectively felt that she had no other choice but to sign the agreement.

b. No other alternatives

Whether circumstances permitted any other reasonable alternative to accepting the settlement agreement terms and signing a release is an objective determination. *Northern Fabrication Co., Inc. v. UNOCAL*, 980 P.2d 958, 960 (Alaska 1999). "What constitutes a reasonable alternative is a question of fact, depending on the circumstances of each case." *Totem Marine*, 584 P.2d at 22. For example, an available legal remedy, such as an action for breach of contract, may provide a reasonable alternative. *Id.* When one party wrongfully threatens to withhold money from another unless certain demands are met, the availability of other sources of funds may also provide an alternative to accepting the coercing party's terms. *Id.* "[T]he adequacy of the remedy is to be tested by a practical standard which takes into consideration the exigencies of the situation in which the alleged victim finds [her]self." *Id.* (citations omitted). If pursuing an available remedy leads to a delay that would cause immediate and irreparable loss to one's economic or business interest, it may be inadequate. *Id.*

Maude will argue that the various actions taken by the City deprived her of income and partially led to her inability to leave Stormy. The City seized Maude's tools, preventing her from operating Buoy Boats, and fired her from her job. Based on the statements made by the City police officers serving the writ and the StormyAir ticketing agent, Maude believed that any ticket she purchased might be subject to execution under state law and that she would not be allowed on a plane without permission from Calvin, the City's attorney. Arguably, Maude may have had alternatives to executing the settlement agreement in order to obtain an airline ticket which would not be seized pursuant to the writ. Maude could have approached Calvin and asked whether he had any intention of seizing any ticket or she could have attempted to purchase a ticket to see whether it would have been seized. Maude could have contacted an attorney and asked for advice or attempted to arrange some alternate form of transportation. However, the adequacy of the alternatives must be tested by a practical standard taking into the exigencies of the situation in which Maude found herself. Stormy is a remote island where passenger air service is offered only two days per week. Maude's mother was gravely ill and Maude believed that she had to get to Anchorage quickly. This placed Maude in a much weaker bargaining position than that of the City, which is one of the *Schmidt* factors in favor of voiding the settlement. *Schmidt*, 627 P.2d at 204, n. 8. Finally, Maude was not represented by an attorney when she signed the agreement and the agreement was prepared and signed within hours of the suit being filed.

c. Coercive acts

The third prong of the test embodies two requirements: (1) coercive acts on the part of the other party and (2) a causal link between the coercive acts and the circumstances of the releasing party's duress. *Zeilinger v. SOHIO Alaska Petroleum Co.*, 823 P.2d 653, 658 (Alaska 1992). The court in *Helstrom* noted that this prong has been "liberally construed, requiring that the strained circumstances be the result of acts which are criminal, tortious, or even merely 'wrongful in the moral sense.'" *Helstrom*, 797 P.2d at 1198 (citing *Wassink v. Hawkins*, 763 P.2d 971, 974 (Alaska 1988)). That being said, a party "is not allowed to use its financial weakness as a sword to negate a properly executed release" and therefore must prove that the coercive party's conduct caused the circumstances of duress.

Maude's duress allegations are based on the City's actions, which had the effect of depriving her of income and preventing her from leaving Stormy. Maude claims that when the City seized all of her tools, she was no longer able to operate Buoy Boats. After being fired, Maude was functionally left with no means of supporting herself. Examinees should recognize, however, that the acts by the City which prevented Maude from earning income did not interfere with Maude's ability to leave the island. After signing the settlement agreement, Maude remained liable to the City for \$10,000 and transferred ownership of her tools. Therefore, the settlement didn't restore Maude's ability to generate income and it wasn't her financial situation which prevented her from leaving the island because even without any source of income, Maude was able to secure funds to purchase a plane ticket and leave Stormy. Therefore, the actions taken by the City that had the result of depriving Maude of income did not, by themselves, prevent her from leaving Stormy. It is just as plausible for examinees to argue that Maude's own actions of converting City property to her own use led to the City's actions, and find no causal connection between the coercive acts and the circumstances of the duress.

Maude may still be able to satisfy the coercive acts prong of the test by coupling her financial situation with her stated belief that even if she had money to purchase a plane ticket she would not be allowed to leave Stormy without first settling with the City. The City police officers serving the writ explained to Maude that any plane ticket she purchased would be subject to execution, and the StormyAir ticketing agent did not merely confirm that, but instead told Maude that she would not be allowed on a plane without permission from Calvin, the City's attorney. Even though Calvin contends that the City had no intention to seize any airline tickets, he does not dispute that he spoke with the StormyAir ticketing agent, and there is an argument to be made that a reasonable person would believe that the only way she could leave the island was by signing the settlement agreement. Under this argument, it is likely that the City caused Maude's plight through acts that were at least "wrongful in the moral sense." *See Helstrom*, 797 P.2d at 1199 (citing *Totem*

Marine, 584 P.2d at 22).

It is just as legitimate for examinees to argue the opposite position, that the City's acts were not "wrongful in the moral sense." The question instructs the examinees that the writ was validly issued. While the City may have aggressively pursued its legal remedies, it did so within the letter of law and should not be penalized for doing so.

2. Is the liquidated damages clause in the settlement agreement valid? Discuss. (40 points)

Maude has a strong argument that the liquidated damages provision in the settlement agreement is unconscionable. The Alaska Supreme Court adopted the Restatement (Second) of Contracts § 208 standard of unconscionability in *Vockner v. Erickson*, 712 P.2d 379, 381-83 (Alaska 1986). The Restatement identifies factors that support a finding of unconscionability, such as "weakness in the contracting process like those involved in more specific rules as to contractual capacity, fraud, and other invalidating causes," "gross disparity in the values exchanged," and "gross inequality of bargaining power." Restatement (Second) of Contracts § 208 comment a at 107-108, comment d at 109 (1981).

To void a contract or provision of a contract for unconscionability, "a sliding scale is invoked which disregards the regularity of the procedural process of the contract formation, that creates the terms, in proportion to the greater harshness or unreasonableness of the substantive terms themselves." *Vockner*, 712 P.2d at 383 (citations omitted).

Parties to a contract are free to stipulate in advance to an amount that would be paid as compensation for a loss or injury flowing from a breach of the contract. The crucial question regarding enforcement of a liquidated damages clause is whether the stipulated amount is a reasonable pre-contract estimate of actual damages or is an illegal penalty. "A valid liquidated damages clause is an agreement to set in advance damages for breach which would otherwise be difficult to determine. However, the clause may not set damages so as to penalize the breaching party for the breach, without regard to the harm caused by the breach." *Helstrom*, 797 P.2d at 1200 (citations omitted).

Alaska has adopted a two-step test for liquidated damage clause enforceability. Liquidated damages are proper (1) where it would be difficult to ascertain actual damages, and (2) where the liquidated amount is a reasonable forecast of the damages likely to occur in the event of a breach. *Carr-Gottstein Properties, Ltd. Partnership v. Benedict*, 72 P.3d 308 (Alaska 2003) (citations omitted); see also *Southeast Alaska Constr. Co., Inc. v. State*, 791 P.2d 339, 343 (Alaska 1990).

Like the liquidated damages provision in *Helstrom*, the provision in Maude's settlement agreement with the City, entitling the City to \$10,000 in the event of a breach, seems unconscionable. The settlement agreement in this fact pattern allows the City to pursue the actual damages of a breach by freeing it to litigate its claims against Maude and by requiring Maude to pay all attorney's fees associated with that litigation. The liquidated damages provision then gives the City an *additional* \$10,000 in damages. The liquidated damages clause more closely resembles a penalty for breach rather than a "reasonable forecast of damages likely to occur in the event of a breach." *Id.*