ESSAY QUESTION NO. 3

Answer this question in booklet No. 3

Gold Nuggets, LLC (Nuggets) is the manufacturer of *Alaskan Gold,* moose pellets collected and spray painted with gold paint by *Nuggets* to satisfy the demand of the tourism industry for all things Alaskan. *Nuggets* operated out of a factory on 1st Avenue in Anchorage that it leased from *Big Wild Property, Inc.* (*Property*) in August, 2006. At the time the five-year lease was entered into by the parties, the lease for the factory included all the machinery needed to process the pellets and produce the *Alaskan Gold*.

In 2007 and 2008 *Nuggets* earned good profits and was also the best tenant *Property* had ever had in this rented space. In 2009 *Nuggets'* business exploded – literally. The pellets had been stored in a room without any ventilation, and the buildup of methane gas in May and June of 2009 resulted in spontaneous combustion on July 4, 2009. While the building survived, the machinery inside the factory was destroyed. The lease included a "calamity clause" which provided that in the event of a calamity such as this one, the lease would terminate unless the parties to the lease agreed otherwise. Following the explosion *Nuggets* notified *Property* of its intent to relocate.

Valuing *Nuggets* as a tenant, *Property* offered to replace all the damaged machinery if *Nuggets* would continue to lease the space under the existing terms. Happy with the terms of its lease but sensing an opportunity to improve its commercial position, *Nuggets* orally agreed to continue the lease if the machinery could be replaced with top-of-the-line equipment and could be running by August 15, 2009 so that the annual gathering and preparation of the pellets could occur before snowfall. Spray painting of the pellets must occur within seven days of the date the pellets are collected or the spray paint will not adhere to the surface of the pellets. *Property* was aware that failure to have the machinery up and running in time to collect and paint the moose pellets before snowfall would prohibit *Nuggets* from producing an inventory for the next year.

Property agreed to purchase top-of-the-line equipment and to have it installed as quickly as possible by a satisfactory vendor. By July 10, 2009, *Property* had identified a vendor, *Anchorage Machinery Replacers, LLP* (*AMR*). *Property* instructed *Nuggets* to work with *AMR* to identify the necessary machinery for purchase and placement. Once *Nuggets* had identified the machinery and diagramed the appropriate locations for placement for *AMR*, *Property* contracted with *AMR* for the purchase of the machinery and *AMR* warranted to *Property* that the equipment would be in place by September 1, 2009 and would perform in accordance with industry standards.

On September 10, 2009, at a cost to *Property* of more than $1.5 million, all machinery was finally in place and collection of the moose pellets began. The machinery repeatedly stopped running, however, such that it was virtually impossible for *Nuggets* to process the inventory needed for 2010. On October 1, 2009 Anchorage received the largest snowfall on record for a single date. The snowfall was followed immediately by extremely low temperatures such that the initial snowfall did not melt for the rest of the winter. *Nuggets* was forced to close down its business.

Nuggets filed a lawsuit the following spring against *Property* and *AMR*, claiming that *Property* had breached its contract with *Nuggets* by failing to deliver the factory in operating condition by August 15, 2009, and that *AMR* had breached its contract with *Property* by not having the machinery up and running on time.

1. Discuss whether an enforceable contract was created requiring delivery of the factory and machinery by *Property* by August 15, 2009.

2. Discuss whether *Nuggets* has a claim against AMR for breach of contract.

GRADER'S GUIDE

*****QUESTION NO. 3*****

SUBJECT: CONTRACTS

1. **Discuss whether an enforceable contract was created requiring delivery of the factory and machinery by *Property* by August 15, 2009. (60 points).**

The formation of an express contract requires "an offer encompassing its essential terms, an unequivocal acceptance of the terms by the offeree, consideration and an intent to be bound." *Wyatt v. Wyatt*, 65 P.3d 825, 828 (Alaska 2003); *Young v. Hobbs*, 916 P.2d 485, 488 (Alaska 1996); *Hall v. Add-Ventures, Ltd.*, 695 P.2d 1081, 1087 n.9 (Alaska 1985).

The parties had an existing contract which provided that in the event of a calamity such as the one experienced here, the lease would terminate unless the parties agreed otherwise. *Nuggets* promptly notified *Property* of its intent to relocate, consistent with the calamity clause. *Property* then extended an offer for a new contract.

(1) The Offer and Acceptance.

Concerned with the potential loss of its tenant, *Property* extended the following offer: We will replace the machinery if you will continue to lease the factory. "Mutual assent is an elementary requirement for a binding contract." *Zeman v. Lufthansa German Airlines*, 699 P.2d 1274, 1281 (Alaska 1985) (citing *State v. Fairbanks North Star Borough School District*, 621 P.2d 1329, 1331 n. 3 (Alaska 1981)). And in order for a new contract to have been formed, it was necessary that the acceptance be unequivocal and in exact compliance with the requirements of the offer. *Walton v. Ramos Aasand & Co.*, 963 P.2d 1042, 1046 (Alaska 1998); *Valdez Fisheries Development Ass'n, Inc. v. Alyeska Pipeline Service Co.*, 45 P.3d 657, 665 (Alaska 2002).

Nuggets did not accept *Property's* offer unequivocally and in exact compliance with the offer. They added two terms. First, *Nuggets* would continue to lease the property if *Property* would replace the damaged equipment with top-of-the-line equipment. Second, *Nuggets* would continue to lease the property if *Property* would have the factory up and running no later than August 15, 2009.

A reply to an offer which purports to accept the offer 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. <u>Restatement (Second)</u>

____________ §59 (1979). *Nuggets* made a counter-offer: We will stay if you will replace the machinery and have it operating and available by August 15, 2009. *See Southwest Marine, Inc. v. State, Dep't of Transp. and Public Facilities, Div. of Alaska Marine Highway Systems*, 941, P.2d 166, 173 (Alaska 1997). Thus, there was no contract at this point.

Property did not "unequivocally accept" the terms of Nuggets' counter-offer, either. Property agreed to one term – replacement of the damaged equipment with top-of-the line equipment. But it rejected the second term and replaced it with another – the factory would be available with the new equipment "as quickly as possible by a satisfactory vendor." Another counter-offer was therefore made.

Unless otherwise indicated by the offeror, an offer invites acceptance by any medium reasonable in the circumstances. <u>Restatement (Second) of Contracts</u>, §30. *Property* has offered to replace the machinery, with timing of the completion of the project dependent on the vendor's schedule, and it invited acceptance by performance by suggesting that *Nuggets* work with *AMR* to complete the project – a request that was acted on by *Nuggets*. The examinee is told that *Nuggets* identified the necessary equipment and diagramed the locations it would need to be placed in the factory.

Thus, *Property* did not agree to deliver the working factory by August 15, 2009 and there was no enforceable contract to do so. This was a request by *Nuggets* that was not accepted. *Nuggets* did, however, accept *Property's* offer to replace the machinery as quickly as possible and to continue the lease.

(2) Consideration.

"Consideration" may be either detrimental reliance or benefit to the promisor. The consideration given by *Property* to conclude the contract may be identified in the form of the money spent on the new equipment. Detrimental reliance may also be identified on the part of *Nuggets* in foregoing relocation in order to comply with the terms of the offer.

(3) Intent to be bound.

The expense paid by *Property* and the decision to forego relocation by *Nuggets* demonstrate an intent to be bound.

A contract was formed requiring that the factory be available as quickly as possible, but not necessarily by August 15, 2009.

Discussion regarding the statute of frauds.

The agreement concerning the repair of the factory relates to the lease executed by *Nuggets* and *Property* in 2006, which automatically terminated unless otherwise agreed by the parties. The subsequent agreement was not in writing, so an examinee may raise the statute of frauds as a basis for contesting enforceability of the new contract.

AS 9.25.010(a) provides that where "an agreement by its terms is not to be performed within a year of the making of it," the agreement is unenforceable unless it or some note or memorandum of it is in writing and subscribed by the party charged. The statute of frauds has been uniformly interpreted to place substance over form. It has not been construed to require a formal or complete written contract and should be flexibly applied on a case-by-case basis to accept any writing that realistically dispels the danger of fraud. 2 Arthur Linton Corbin, *Corbin on Contracts* §498, at 681 (1950), as quoted in *Fleckenstein v. Faccio*, 619 P.2d 1016, 1020 (Alaska 1980). "We should always be satisfied with some note or memorandum that is adequate, when considered with the admitted facts, the surrounding circumstances, and all explanatory and corroborative and rebutting evidence, to convince the court that there is no serious possibility of consummating a fraud by enforcement." *Fleckenstein*, 619 P.2d at 1020.

A statute of frauds defense would probably be unsuccessful. Where the landlord and the tenant had executed a lease and the agreements concerning the repairs were subsequent to the lease and addressed only the terms under which the parties agreed to continue under the same lease, there was a writing with the essential terms contained in it. There is slim opportunity for perpetrating a fraud on the court in this instance.

2. Discuss whether *Nuggets* has a claim against *AMR* for breach of contract. (40 points)

As a preliminary matter, note that the only contract entered into by *AMR* was with *Property*. And there were no representations or warranties made by *AMR* directly to *Nuggets*. Therefore, the only basis for a breach of contract claim by *Nuggets* against *AMR* must arise on the theory that *Nuggets* is a third-party beneficiary of the contract between *AMR* and *Property*.

The key issue is whether or not *Property* and *AMR* intended for *Nuggets* to be a beneficiary of their contract. *See Howell v. Ketchikan Pulp. Co.,* 943 P.2d 1205, 1207 (Alaska 1997). The sole purpose of the contract need not be for the benefit of *Nuggets*, but the parties must either have intended or contemplated that one purpose of the contract would be to benefit *Nuggets*. *Century Ins. Agency, Inc. v. City Commerce Corp.*, 396

P.2d 80, 82 (Alaska 1986). The intent of the parties, including those of the promissee, are determinative. *Id.* The benefit to *Nuggets* cannot be simply incidental, though. *Id.*

Nuggets will argue:

- The machinery purchased and installed was for the benefit of *Nuggets*;
- *Nuggets* negotiated to have the top-of-the-line machinery installed, rather than simple replacement of the original machinery;
- The installation of the new machinery was a term precedent to continuing the lease;
- *Property* instructed *Nuggets* to work with *AMR* to achieve the purchase and installation;
- *Nuggets* took control of the factory and attempted to operate the machinery, which would have been to its benefit.
- *AMR*, by virtue of its communication and coordination with *Nuggets*, knew that the contract was for the benefit of *Nuggets* as evidenced by the fact that they acted on the information obtained through the communication and coordination.

A strong argument exists that *Property* was trying to fulfill its obligation to *Nuggets* by contracting with *AMR* for the purchase and installation of the new equipment and that absent its intent to fulfill that obligation it would not have incurred the higher expense associated with the top-of-the line machinery. *Property* agreed to purchase top-of-the-line equipment and have it installed as quickly as possible specifically because of the need to have it ready to process pellets before snowfall, and the contract with *AMR* was a means to that end. *See Kennedy Associates, Inc. v. Fischer*, 667 P.2d 174, 178 (Alaska 1983) (holding that where a promissor under a contract seeks to discharge its obligations to a third party by the promissor's performance under the contract, there is no question but that the third party is an intended third-party beneficiary). In other words, where a promissor under a contract seeks to discharge its obligations by entering into a second contract with another entity to perform the obligation to the promisee, there is no question but that the original promissee is a third-party beneficiary of the second contract.

AMR will certainly argue that there is no evidence of an intent to benefit *Nuggets*, and it is likely to point to the lack of warranties made directly to *Nuggets*, the limited time left on the lease, the amount *Property* spent on the renovations despite the limited time remaining on the lease, and the lack of any reference to *Nuggets* in the contract between *AMR* and *Property*.

It is unclear how a jury would decide this question given the arguments available to both parties. The examinee should receive credit for arguing both sides.