

1986

The Freedom Not to Contract

Wendell H. Holmes

Louisiana State University Law Center, wendell.holmes@law.lsu.edu

Follow this and additional works at: https://digitalcommons.law.lsu.edu/faculty_scholarship



Part of the Law Commons

Repository Citation

Holmes, Wendell H., "The Freedom Not to Contract" (1986). *Journal Articles*. 338.
https://digitalcommons.law.lsu.edu/faculty_scholarship/338

This Article is brought to you for free and open access by the Faculty Scholarship at LSU Law Digital Commons. It has been accepted for inclusion in Journal Articles by an authorized administrator of LSU Law Digital Commons. For more information, please contact kreed25@lsu.edu.

THE FREEDOM NOT TO CONTRACT

WENDELL H. HOLMES*

The Anglo-American legal tradition has long espoused the view that contracts are creations of the exercise of mutual assent. General rules of offer and acceptance require that the parties clearly manifest their intent to be bound. This manifestation ordinarily takes the form of promises, either express or implied, by each party to the other. This truism is subject to an important, although not necessarily inevitable, qualification: that the parties will be required to act in accordance with the manifestations of their intent measured by an objective standard.¹ In the terminology of traditional contract law,² it is the

* Associate Professor of Law, University of Mississippi. B.A. 1974, Millsaps College; J.D. 1977, Tulane University.

1. See *RESTATEMENT (SECOND) OF CONTRACTS* §§ 2, 4, 17-24, 26, 35 (1979). This discussion presupposes the existence of what has traditionally been called a bilateral contract, in which both parties exchange promises. The necessary manifestation of intent can, of course, take the form of performance in a unilateral contract. *Id.* § 18. The Second Restatement abandons the bilateral-unilateral dichotomy in nomenclature.

2. For purposes of this article, the definitions of "classical contract law," "neoclassical contract law" and "traditional contract law" are those suggested by Professor Ian Macneil. By classical contract law Macneil refers to the theoretical structure associated with Samuel Williston. This structure is best expressed in Professor Williston's multi-volume treatise and the Restatement of Contracts (1932), for which he served as reporter. Neoclassical contract law describes the significant modifications of that structure represented by Article 2 of the Uniform Commercial Code and the Restatement (Second) of Contracts (1979). I would add as an essential precursor to both the treatise of Arthur Corbin, whose work heavily influenced both the U.C.C. and Second Restatement. Macneil has used the term traditional contract law to encompass both classical and neoclassical doctrine. See Macneil, *Contracts: Adjustment of Long-Term Economic Relations Under Classical, Neoclassical, and Relational Contract Law*, 72 *Nw. U.L. REV.* 854, 855 n.2 (1978).

This article uses the term traditional contract law because neither classical nor neoclassical theory differs significantly in its treatment of the issues discussed herein. However, the following "traits" of classical contract theory should be noted:

- 1) an emphasis on contractual liberty manifested in a noninterventionist governmental posture and premised on the equality of bargaining power necessary to make this freedom meaningful; 2) a tendency toward relativism and subjectivism displaying itself in a general lack of concern with good faith, fair dealing, and substantive justice; 3) a formalism expressing itself in a system of autonomous, abstract, precise, general, and mechanical rules; and 4) a wide social sweep, created by its tendency to take over areas of life now governed by other legal doctrines. Permeating all these traits was classical contract law's

reasonable person's interpretation of the promisor's intent that is of paramount significance, rather than the promisor's unexpressed, subjective beliefs.³ So long as the promisee both honestly and reasonably believes that the promisor intends to be bound, the law deems the requisite assent to be present.⁴

From this fundamental proposition, traditional contract law proceeded to a corollary principle: regardless of the form of his promise, so long as a party manifests with sufficient clarity his intention *not* to be bound, then no legally enforceable obligations can result.⁵ Thus, what in every other sense would be considered a binding contract could, by use of appropriate language, be transformed into a "gentlemen's agreement" evidencing a moral obligation, "enforceable" only by the sanction of honor rather than the processes of law.⁶ According to traditional contract theory, then, the freedom of contract carried with it a correlative freedom not to contract. The logic would seem irrefutable: if all contracts are promises,⁷ then those promises that

main defining feature: its emphasis on freedom.

Metzger & Phillips, *The Emergence of Promissory Estoppel as an Independent Theory of Recovery*, 35 RUTGERS L. REV. 472, 501 (1983).

3. See RESTATEMENT (SECOND) OF CONTRACTS § 2(1) & comment c (1979) (defining promise as "a manifestation of intention to act or refrain from acting in a specified way, so made as to justify a promisee in understanding that a commitment has been made"). A classic formulation of the objective theory was given by Judge Learned Hand in *Hotchkiss v. National City Bank*, 200 F. 287, 293 (S.D.N.Y. 1911):

A contract has, strictly speaking, nothing to do with the personal, or individual, intent of the parties. . . . If . . . it were proved by twenty bishops that either party, when he used the words, intended something else than the usual meaning which the law imposes on them, he would still be held, unless there were some mutual mistake, or something else of the sort.

4. The promisee, then, must not only be justified in an objective sense in believing that the promisor made an offer; he must also honestly (*i.e.*, subjectively) believe that this was the promisor's intent. If either element is lacking, no enforceable offer has been made. See, *e.g.*, *Lucy v. Zehmer*, 196 Va. 493, 84 S.E.2d 516 (1954).

5. This is true both in the United States and in England. See, *e.g.*, W. ANSON, ANSON'S LAW OF CONTRACT 66-67 (A. Guest 25th ed. 1979); CHESHIRE & FIFOOT'S LAW OF CONTRACT 102-04 (M. Furmston 10th ed. 1981); 1 A. CORBIN, CORBIN ON CONTRACTS § 34 (1963); J. MURRAY, MURRAY ON CONTRACTS § 20, at 31 (2d rev. ed. 1974); 1 S. WILLISTON, A TREATISE ON THE LAW OF CONTRACTS § 21 (W. Jaeger 3d ed. 1957).

6. A. CORBIN, *supra* note 5, § 34.

7. See RESTATEMENT (SECOND) OF CONTRACTS § 1 (1979) (defining contract as "a promise or a set of promises for the breach of which the law gives a remedy, or the performance of which the law in some way recognizes as a duty"). In this sense contracts may be categorized as a subset of all promises, *i.e.*, those promises that are legally enforceable. See Lightsey, *A Critique of the Promise Model of Contract*, 26 WM. & MARY L. REV. 45 (1984).

create contracts can be negated by express declarations that they do not bind the promisor.

The "promise model"⁸ embraced by traditional contract law has had no shortage of critics.⁹ It is hardly revolutionary to suggest that no unitary law of contract now exists, if indeed it ever did. There is, however, no consensus regarding what has supplemented, or perhaps supplanted, the regime of consent. The most notable and obvious theory is that detrimental reliance may obtain independent standing with intent in the pantheon of contractual obligations.¹⁰ Others have argued that the results of modern contract cases may be more accurately described in terms of the status of the parties than the requirements of the promise model.¹¹ A strong trend in alternative contract theory views the relationships between contracting parties as generating their respective rights and obligations.¹² Nonetheless, arguably

8. This article uses the term "promise model" to describe the theoretical construct established by the two Restatements for the enforcement of contracts. This construct centers upon the traditional rules governing offer, acceptance, and consideration.

9. By the same token, it is not without its defenders, at least in the sense of those who view promise as the primary component of contract. The outstanding example is Professor Charles Fried, whose recent book argues that contracts are enforceable because promises are morally binding on those who make them. C. FRIED, *CONTRACT AS PROMISE* (1981); see also Blum & Wellman, *Participation, Assent and Liberty in Contract Formation*, 1982 ARIZ. ST. L.J. 901 (arguing that freedom of contract is a liberty protected by state and federal constitutions and that mutual assent is the fundamental standard of contract obligation); Goetz & Scott, *Enforcing Promises: An Examination of the Basis of Contract*, 89 YALE L.J. 1261 (1980) (arguing that substantial congruence exists between traditional contract rules and optional promissory enforcement).

10. I make no attempt to enumerate exhaustively those who have either suggested or espoused the theory that reliance is at least an alternative to promissory obligation; for a recent comprehensive survey of this position, see Metzger & Phillips, *supra* note 2. The Second Restatement, while grounded in the promise theory, is replete with references to the reliance concept. The most obvious of these is section 90 (promissory estoppel); other provisions dealing with reliance include sections 34, 87, 89, 139, 349 and 377. For a detailed discussion of this issue, see Knapp, *Reliance in the Revised Restatement: The Proliferation of Promissory Estoppel*, 81 COLUM. L. REV. 52 (1981). See also Fuller & Perdue, *The Reliance Interest in Contract Damages*, 46 YALE L.J. 52, 373 (1937) (a seminal work widely credited with bringing the question of reliance-based injuries to the forefront of the modern law of contract damages, thereby focusing attention on the general issue of detrimental reliance).

11. See, e.g., Childres & Spitz, *Status in the Law of Contract*, 47 N.Y.U. L. REV. 1 (1972); cf. Radin, *Contract Obligation and the Human Will*, 43 COLUM. L. REV. 575 (1943) (discussing the prominence of nonpromissory or "compulsory" obligations in modern society); Reh binder, *Status, Contract, and the Welfare State*, 23 STAN. L. REV. 941 (1971) (arguing that modern law relates to persons primarily in the context of their social roles).

12. Professor Fried characterizes this theory as follows:

the most influential contemporary authority, the *Restatement (Second) of Contracts*, accepts the promise model and reaffirms the freedom not to contract, albeit somewhat diffidently: "Neither real nor apparent intention that a promise be legally binding is essential to the formation of a contract, but a manifestation of intention that a promise shall not affect legal relations may prevent the formation of a contract."¹³

On this view, contractual relations establish ties of community between the parties, and such ties generate their own moral imperatives, quite apart from the limited obligations the parties may have assumed in creating the relation. . . . [T]his view does not hold that a set of obligations is imposed on the parties by society for general social purposes; but rather, the relationship itself is seen as implying moral duties and constraints.

C. FRIED, *supra* note 9, at 76. He includes Professors Macneil, Fuller, Gilmore, Kessler, and Atiyah as prominent advocates of this view. *Id.* Significant works by those authors include P. ATIYAH, *PROMISES, MORALS AND LAW* (1981) [hereinafter cited as P. ATIYAH, *PROMISES*]; P. ATIYAH, *THE RISE AND FALL OF FREEDOM OF CONTRACT* (1979) [hereinafter cited as P. ATIYAH, *RISE AND FALL*]; L. FULLER, *ANATOMY OF THE LAW* (1968); G. GILMORE, *THE DEATH OF CONTRACT* (1974); I. MACNEIL, *THE NEW SOCIAL CONTRACT* (1980) [hereinafter cited as I. MACNEIL, *SOCIAL CONTRACT*]; Kessler & Fine, *Culpa in Contrahendo, Bargaining in Good Faith and Freedom of Contract: A Comparative Study*, 77 *HARV. L. REV.* 401 (1964); Macneil, *The Many Futures of Contracts*, 47 *S. CAL. L. REV.* 691 (1974) [hereinafter cited as Macneil, *Many Futures*]; cf. S. WILLISTON, *supra* note 5, § 32a, at 89-90 (discussing relational duties existing at common law).

13. RESTATEMENT (SECOND) OF CONTRACTS § 21 (1979) (emphasis added). The comments elaborate on this proposition:

Parties to what would otherwise be a bargain and a contract sometimes agree that their legal relations are not to be affected. *In the absence of any invalidating cause*, such a term is respected by the law like any other term, but such an agreement may present difficult questions of interpretation: it may mean that no bargain has been reached, or that a particular manifestation of intention is not a promise; it may reserve a power to revoke or terminate a promise under certain circumstances but not others. In a written document prepared by one party it may raise a question of misrepresentation or mistake or overreaching; to avoid such questions it may be read against the party who prepared it.

The parties to such an agreement may intend to deny legal effect to their subsequent acts. But where a bargain has been fully or partly performed on one side, a failure to perform on the other side may result in unjust enrichment, and the term may then be unenforceable as a provision for a penalty or forfeiture. . . . In other cases the term may be unenforceable as against public policy because it unreasonably limits recourse to the courts or as unconscionably limiting the remedies for breach of contract.

Id. comment b (emphasis added).

Section 21 was incorporated unchanged (although renumbered) from the original draft of the Second Restatement. See RESTATEMENT (SECOND) OF CONTRACTS § 21B (Tent. Draft No. 1, April 13, 1964). It had no direct counterpart in the First Restatement, perhaps an indication that to Professor Williston, the reporter, the concept that one is free to negate contractual obligations by appropriate expressions was so self-evident that restating it was superfluous. Certainly Williston, the paragon contracts classicist, held no doubts as to its viability: "It is indeed true that if the parties to an agree-

This article seeks to consider the continued viability of this freedom not to contract¹⁴ through examination of the most common situations where “no-binding-effect” clauses are utilized: employer-employee agreements involving bonuses, pensions, and death benefits,¹⁵ and the “letters of intent” or “memoranda of understanding” frequently executed in commercial settings.¹⁶ An analysis of these cases suggests that, contrary to traditional dogma, such clauses are not regularly enforced by courts on any systematic basis. The article examines the means by which courts avoid giving effect to such clauses, and their reasons—either apparent or real—for so doing. The discussion attempts to determine why parties continue to include such clauses in their agreements, and whether any useful purpose is

ment undertake that no legal obligation shall be created, their undertaking in this regard will be respected by the law, as would any other term of their agreement, provided neither the agreement nor the stipulation itself is illegal.” S. WILLISTON, *supra* note 5, § 21, at 39-41. This article will examine the extent of the law’s “respect” for such undertakings, as well as consider how strenuously courts seek the “invalidating causes” referred to in comment b above.

The First Restatement did address the issue of statements of intention that do not constitute offers, but in a far broader context than that of section 21 of the Second Restatement. The language of the First Restatement makes an interesting comparison to section 21:

If from a promise, or manifestation of intention, or from the circumstances existing at the time, the person to whom the promise or manifestation is addressed knows or has reason to know that the person making it does not intend it as an expression of his fixed purpose until he has given a further expression of assent, he has not made an offer.

RESTATEMENT OF CONTRACTS § 25 (1932); *see also id.* § 20 (neither mental assent to promises nor real or apparent intent to be bound is essential). The circumstances that may create actual or constructive knowledge of the promisor’s intent not to be bound are myriad. This article is limited to those situations where an *express* declaration of purpose has been made. For distinctions of other types of cases, *see infra* note 17.

14. In addition to the Second Restatement, two recent and widely-used contracts treatises, those of Professor Farnsworth and Professors Calamari and Perillo, accept this principle with little or no qualification. According to Farnsworth, under the objective theory, a court will honor a party’s intention that his promise have no legal consequences if the other party knows or has reason to know it. E. FARNSWORTH, *CONTRACTS* § 3.7, at 116 (1982). Thus, he concludes:

The easiest way for a party to make clear his intention not to be legally bound is to say so. In a number of commercial contexts, parties enter into “gentlemen’s agreements” that state that they are not legally binding, and it is beyond question that the parties can in this way turn an otherwise enforceable agreement into an unenforceable one.

Id. at 117. Professors Calamari and Perillo are essentially in accord. *See* J. CALAMARI & PERILLO, *THE LAW OF CONTRACTS* § 6-11, at 216 (2d ed. 1977).

15. *See infra* notes 18-78 and accompanying text.

16. *See infra* notes 79-129 and accompanying text.

served by doing so. Since my conclusion suggests that there has been a deterioration of the promise model of contracts, the article will consider whether the outcome of these cases may be more accurately explained by alternative theories of contractual obligation. The conclusion reformulates the current status of the freedom not to contract.¹⁷

17. It should be noted that this article does not purport to be an exhaustive survey of cases on point, and attempts no quantificational analysis. The basic methodology employed is examination of representative cases within each category and of subsequent cases dealing in some fashion with no-binding-effect clauses which, in many instances, cite one or more of the principal cases as authority. For other collections of some of the categories of cases discussed herein, see Note, *Contractual Aspects of Pension Plan Modification*, 56 COLUM. L. REV. 251 (1956); Note, *Legal Problems of Private Pension Plans*, 70 HARV. L. REV. 490 (1957); Note, *Consideration for the Employer's Promise of a Voluntary Pension Plan*, 23 U. CHI. L. REV. 96 (1955); Annot., 46 A.L.R.3D 464 (1972); Annot., 42 A.L.R.2D 461 (1955).

Certain other issues, related to but outside the purview of this article, should be noted at this point. First, this article is not concerned with the enforceability of so-called "agreements to agree," i.e., an agreement which the parties intend to express an existing obligation but which leaves one or more terms to be resolved by future negotiation. These agreements will often be treated as unenforceable on grounds that a court should not contract for the parties or bind them to terms upon which they were unable to agree. See, e.g., *Walker v. Keith*, 382 S.W.2d 198 (Ky. 1964) (renewal option in lease providing for rental to be agreed upon on the basis of "comparative business conditions" of the two lease periods held invalid). *Contra* *Greene v. Leeper*, 193 Tenn. 153, 245 S.W.2d 181 (1951) (renewal option in lease leaving rental to be agreed upon according to "business conditions" at the time of renewal valid and enforceable; rental value subject to proof by expert testimony). Courts that refuse to enforce such agreements essentially treat the failure to agree upon the terms left open as evidence of a lack of present assent. J. MURRAY, *supra* note 5, § 27. The Uniform Commercial Code has significantly alleviated such problems in contracts for the sale of goods. See, e.g., U.C.C. § 2-204(3) (1978); J. WHITE & R. SUMMERS, *HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE* §§ 3-1 to 3-9 (1972). The Second Restatement applies many of the U.C.C. concepts in this area to contracts generally. See *RESTATEMENT (SECOND) OF CONTRACTS* §§ 33-34 (1979). See generally Knapp, *Enforcing the Contract to Bargain*, 44 N.Y.U. L. REV. 673 (1973).

A second category of cases outside of the parameters of this article is the "formal contract contemplated" cases. Typically these cases involve parties who negotiate a transaction with the expectation that they will ultimately sign a formal document setting forth the specific terms of their agreement. During the process of negotiation, they may reach an oral or written consensus on most, if not all, of the material terms of exchange. In most legal systems, the parties can stipulate by appropriate language that the contemplated writing is constitutive, and that there will be no contract if this writing is not concluded. See 1 R. SCHLESSINGER, *FORMATION OF CONTRACTS: A STUDY OF THE COMMON CORE OF LEGAL SYSTEMS* 178 (1968). If, however, the parties are unable to agree on a formal document and one party sues for breach, a court may be faced with the difficult factual question of whether the parties intended their promises to be legally enforceable before the final document was signed. See, e.g., *Sommer v. Hilton Hotels Corp.*, 376 F. Supp. 297 (S.D.N.Y. 1974). As one might suspect, there is little consistency in the results of such cases. See A. CORBIN, *supra* note 5, § 30; J. MURRAY, *supra* note 5, § 21; L. SIMPSON, *HANDBOOK OF THE LAW OF CONTRACTS* § 17 (2d ed. 1965); S. WILLISTON, *supra*

I. EMPLOYER-EMPLOYEE AGREEMENTS

A. *Death, Pension and Other Benefits*

The most common cases dealing with no-binding-effect clauses in employment relations involve promises by employers to pay death benefits, pensions, severance allowances, and similar benefits. Such inducements indisputably enhance employee performance, loyalty, and goodwill. For obvious reasons, however, employers have long persisted (in the absence of a restraining statute)¹⁸ in describing these benefits as gratuitous, in-

note 5, § 28; Knapp, *supra*.

Clearly, the factual permutations of such cases are limitless; this article includes only those unusual cases where the parties have reduced their agreement to a relatively complete written form but included a no-binding-effect clause foreshadowing the execution of a further document. In this instance, Corbin states that notwithstanding the agreement on all details, the parties may still maintain "complete immunity" from obligation, according to their stated intentions. A. CORBIN, *supra* note 5, § 30, at 98. This article will explore the validity of Professor Corbin's assertion.

Perhaps the most common means of denying present effect to an agreement is the incorporation of express conditions to enforceability. While enforceability may be made conditional on the occurrence of an extrinsic event, in commercial transactions a more common requirement is that one party fulfill objective criteria to the other party's satisfaction. Such conditions may give rise to various factual issues, including questions of good faith, but ordinarily they do not suggest a lack of intent to contract. Thus, many agreements that might include expressions of present unenforceability are excluded from the scope of this article because they link enforceability to the existence of express conditions. A common, industry-wide example in this country is loan commitments. See Draper, *The Broken Commitment: A Modern View of the Mortgage Lender's Remedy*, 59 CORNELL L. REV. 418 (1974); Mehr & Kilgore, *Enforcement of the Real Estate Loan Commitment: Improvement of the Borrower's Remedies*, 24 WAYNE L. REV. 1011, 1015-19 (1978).

Finally, in many cases in which the parties appear to have entered into a binding written contract, one party may challenge the contract on the grounds that both understood that the transaction was a sham. Such cases ordinarily turn on the applicability of the parol evidence rule to evidence supporting that contention, rather than questions of intent. See, e.g., *Kilpatrick Bros. v. International Business Mach. Corp.*, 464 F.2d 1080 (10th Cir. 1972); *Kind v. Clark*, 161 F.2d 36 (2d Cir.), *cert. denied*, 332 U.S. 808 (1947); *Arizona Cotton Ginning Co. v. Nichols*, 9 Ariz. App. 493, 454 P.2d 163 (1969); *McGuire v. Luckenbach*, 131 Colo. 333, 281 P.2d 997 (1955); *Hamilton v. Boyce*, 234 Minn. 290, 48 N.W.2d 172 (1951); *cf. Smith v. MacDonald*, 37 Cal. App. 503, 174 P. 80 (1918) (provision in promissory note that it would be void in the event of transfer or institution of legal collection efforts constituted covenant not to sue).

18. Chief among these, in the area of pensions, is the Employment Retirement Income Security Act of 1974 (ERISA), Pub. L. 93-406, 88 Stat. 829 (codified at 29 U.S.C. §§ 1001-1461 (1982)). In addition, several states have adopted statutes prohibiting employers from terminating pension benefits once the plan requirements for vesting have been met. E.g., N.J. STAT. ANN. § 14A:8-4 (West Supp. 1984). Initially, American courts regarded *all* private pension plans as gratuities that could be withdrawn at any time, even in the absence of no-binding-effect clauses. The broadest implications of the "gra-

tended to create no contract rights, or subject to amendment or revocation at any time. Notwithstanding such qualifying language, to the extent that an employee performs services after such promises, one would suspect that few, if any, cases would so severely test the reach of the objective theory. Yet one recent treatise states that "[g]enerally, the courts have held that reliance on the terms of the offer creates no liability."¹⁹ Certainly, employers have been successful in a surprising number of decisions. An analysis of four well-known cases and their progeny demonstrates, however, that the assertion that employers can generally insulate themselves from liability by the recitation of disclaimers is highly questionable. Indeed, each of the four, *Tilbert v. Eagle Lock Co.*,²⁰ *Schofield v. Zion's Mercantile Institution*,²¹ *Mabley & Carew Co. v. Borden*,²² and *Psutka v. Michigan Alkali Co.*,²³ decided at the height of traditional contract theory,²⁴ held employers liable on promises that were, by any objective analysis, clearly illusory and that unequivocally indicated an "intent" not to be bound.

Tilbert presents the archetypal case. In 1923, the defendant issued to its employee a "Certificate of Benefit" providing for

tuity theory" have been generally discredited, although various grounds for enforcing benefit agreements have been asserted, such as promissory estoppel, unilateral contract, and deferred wages. See B. AARON, LEGAL STATUS OF EMPLOYEE BENEFIT RIGHTS UNDER PRIVATE PENSION PLANS 4-14 (1961); Note, *Pension Plans and the Rights of the Retired Worker*, 70 COLUM. L. REV. 909, 916-21 (1970); Note, *A Reappraisal of the Private Pension System*, 57 CORNELL L. REV. 278, 282-85 (1972) [hereinafter cited as Note, *Reappraisal*].

19. J. CALAMARI & J. PERILLO, *supra* note 14, § 6-11, at 216. The authors acknowledge that "[b]y the process of interpretation of the terms of the offer so as to preclude withdrawal or modification after the employee has retired or died, such promises have been *on occasion* enforced." *Id.* (emphasis added). This article suggests that those occasions have arisen a good deal more frequently than this text would suggest.

20. 116 Conn. 357, 165 A. 205 (1933).

21. 85 Utah 281, 39 P.2d 342 (1934).

22. 129 Ohio St. 375, 195 N.E. 697 (1935), noted in *Contracts—Offer and Acceptance—Effect of Disclaimer of Obligation in Promise to Employee* 49 Harv. L. Rev. 148 (1935) [hereinafter cited as *Contracts*].

23. 274 Mich. 318, 264 N.W. 385 (1936).

24. It also should be noted that these cases arose in the depths of the Great Depression, a time when one should not be overly surprised to find employers seeking to renege on promises. The protection given employees in these cases may be consistent with other efforts, both legislative and judicial, to protect the rights of the disadvantaged during that period of financial exigency. See, e.g., *Home Bldg. & Loan Ass'n v. Blaisdell*, 290 U.S. 398 (1934) (upholding constitutionality of Minnesota's mortgage foreclosure moratorium law).

the payment of a death benefit to the employee's named beneficiary. No consideration was recited. The certificate provided for automatic lapse upon the employee's termination, but more importantly included the following disclaimers:

"This benefit plan being voluntary on the part of Eagle Lock Co., it is understood that it constitutes no contract with any Employee or any beneficiary, and confers no legal rights on him or them. It in no way interferes with his freedom to leave our employ whenever he pleases, nor on the other hand, does it take away our right as Employer to dismiss any Employee."

"We fully expect and hope this benefit plan as outlined above will continue indefinitely and will be appreciated by the Employees to the extent that we feel justified in continuing the plan indefinitely. We must, however, and do reserve to ourselves the right to discontinue these benefits at any time without any liability on our part to any employee or any beneficiary, either or both."²⁵

Thereafter the defendant decided to cancel the certificates effective August 28, 1931 (the next payday). This fact was not communicated to employees until their paychecks were distributed that day with a notice of cancellation attached. Unfortunately for the defendant, the plaintiff's husband had died at 2:00 a.m. on the 28th, several hours before the working day began.

The Supreme Court of Errors of Connecticut had no difficulty in imposing liability on the defendant. Primarily, the court focused upon an ostensible issue of consideration. Declaring that the defendant "must be assumed" to have requested the employee's continued service, the court found a clear acceptance of the death benefit offer in the employee's seven years of service subsequent to the issuance of the certificate. By so doing, he "forebore his right to terminate the employment and engage elsewhere, and conferred the benefit which the defendant sought."²⁶

On the crucial question of intent, the court disposed of the issue by artful interpretation. In its view, the language quoted

25. 116 Conn. at 360-61, 165 A. at 207 (quoting "Certificate of Benefit," schedule B). The court mentioned but did not discuss the fact that the employer had discontinued an existing group life insurance policy concurrently with issuing the certificates. *Id.* at 359, 165 A. at 206.

26. *Id.* at 362, 165 A. at 207.

above involved only the determination whether either party was obligated to continue the employment relationship. Certainly no such obligation existed. To argue, however, that this language meant that the defendant had no liability despite acceptance by the employee prior to the exercise of the reserved power of revocation, "would ascribe to the defendant an intention to mislead its employees, to its advantage, by an inducement which was known and intended by it to be entirely nugatory, and which this record does not require [the court] to attribute to it."²⁷ Thus, the certificate constituted more than an expression of present gratuitous intent—it was, instead, a contract.²⁸

Interestingly, the court did not rely upon vesting, estoppel, restitution, contract implied-in-fact, or related concepts in arriving at this result. Instead its conclusion was based on wholly unsatisfactory reasoning. Even contemporary commentators recognized that, under the classical analysis, consideration is a significant issue only if there is a *promise* designed to induce a reciprocal promise or action. Assuming the fact of promise, it takes but little effort for a court to find a reciprocal action.²⁹ The promise is the fundamental prerequisite, and it exists only

27. *Id.* at 362, 165 A. at 207-08.

28. Somewhat paradoxically, the court concluded that Eagle Lock could discontinue the benefits of their other employees. This is inconsistent with its statement that the "consideration" for the contract was the decedent's continued employment after receiving the certificate. If the defendant were bargaining for an employee's agreement to continue his services, then presumably the "contract" became enforceable at the point that the employee manifested assent; thus, any subsequent attempt to revoke the offer would be ineffective under standard contract principles. If the defendant's offer was construed as seeking service *until death* as acceptance (*i.e.*, an offer for a unilateral contract), the acceptance would have been effective immediately upon the employee's death. In that instance, however, the offer *would* be revocable for those who had not "accepted." See RESTATEMENT (SECOND) OF CONTRACTS § 42 & comment c (1979). The court's dictum on the revocability of the certificates is thus more consistent with the theory that the certificates were continuing offers that could be accepted only by dying while in the defendant's employ. However, this analysis poses the problems of the revocability of offers for unilateral contracts once performance has begun. See *id.* § 45; RESTATEMENT OF CONTRACTS § 45 (1932). Nonetheless, the court's opinion can only be read as saying that had the employee survived 22 more hours, the plaintiff would have lost. The court concluded that the entire day in which a contract expires is open to comply with it; thus, the termination did not become effective until the end of the day on August 28, and death at any time on that day would entitle the beneficiary to recovery. 116 Conn. at 364, 165 A. at 208.

29. See Grismore, *Contracts—Effect of a Stipulation Denying Legal Effect in an Employer's Voluntary Pension, Bonus or Death Benefit Plan*, 34 MICH. L. REV. 700, 702-03 (1936); 49 HARV. L. REV. 148, 149 (1935).

if the intent to be bound is manifested on an objective basis. The court in *Tilbert* ignored this requirement and simply interpreted the defendant's intent to be what the court deemed it should have been.³⁰

The other cases in this group follow similar patterns with identical results, although for purportedly different reasons. *Schofield* involved claims for pension benefits under a noncontributory plan. The plaintiffs had performed under this "gratuitous" plan and had received retirement payments for several years³¹ before the company revised the plaintiffs' allowances and reduced their benefits. The operative language was recited in the company's explanatory brochure:

"15. Neither the action of the Board of Directors in establishing a System of Pensions, nor any other action now or hereafter taken by them or the Board of Pensions in the inauguration and operation of a pension department shall be construed as giving to any officer or employee of the institution a right to be retained in its service, or any right or claim to any pension allowance; and the Institution expressly reserves its right and privilege to discharge at any time any officer or employee when the interest of the Institution in its judgment may so require, without liability for any claim for pension or other allowance than wages due and unpaid."

"16. The Board of Directors reserves the right to change or amend any of the foregoing rules and regulations at any time, and to change the basis of pension allowances by increasing or reducing the same, whenever, in its judgment, the welfare of the Institution may require such change; and the decision of said Board of Directors, in establishing such new basis shall be absolutely conclusive."³²

Focusing upon the substantive provisions of the pension plan, the Supreme Court of Utah found them to encompass all elements of valid offer—not one inviting a verbal acceptance,

30. In Professor Atiyah's words, the court indulged in the time-honored device of surmising that "the parties 'could hardly have intended' that they should not be bound once such-and-such has been done." P. ATIYAH, *RISE AND FALL*, *supra* note 12, at 758.

31. It is noteworthy that the payments apparently came from the company's payroll account. No pension trust or annuity arrangement existed. 85 Utah at 285, 39 P.2d at 346. This factor distinguishes certain earlier cases in which employees were unsuccessful. See *infra* note 35.

32. 85 Utah at 284, 39 P.2d at 343 (quoting resolution establishing pension system).

but one seeking a completed act. Once that act (twenty years of service and attainment of age sixty-five) had been performed, the "contract" was completed and could not be modified at the will of the company.³³ In essence, then, a unilateral contract had been formed.

The court construed the quoted language to give the employer discretion only toward present employees. Citing the general principles of construction that attempt to enforce the purpose of the agreement and favor interpretations that yield valid contracts,³⁴ the court determined that the no-binding-effect clause was inapplicable to a retired employee whose pension rights were "fixed and determined."³⁵

Mabley, the third case in the sequence, involved the claim of the named beneficiary of Anna Work, a deceased employee of Mabley and Carew Company, for payments under a death benefit certificate. That certificate contained the following language:

"The issue and delivery of this certificate is understood to be purely voluntary and gratuitous on the part of this Company and is accepted with the express understanding that it carries no legal obligation whatsoever or assurance or promise of future employment, and may be withdrawn or discontinued at any time by this Company."³⁶

In affirming a judgment for the beneficiary, the Supreme Court of Ohio sidestepped the question of intent. Rather, the "one question" was "the consideration for the issuance of this certificate."³⁷ Since payment would not be made unless the

33. *Id.* at 287-88, 39 P.2d at 344-45.

34. *Id.* at 288, 39 P.2d at 345.

35. *Id.* at 293, 39 P.2d at 347. The court implicitly employed a vesting theory as well as traditional notions of unilateral contracts.

In reaching this resolution, the court was forced to distinguish a number of other decisions where, for various reasons, employees had fared less well. In general those cases fall into two lines, each interesting because the themes involved are common where employees have failed. In one line, the employees failed to satisfy stated eligibility requirements. In the other, the employees' rights were limited to claims against employer-established pension funds administered by third parties. The employees' status as third-party beneficiaries apparently prejudiced their claims; the failure or discontinuance of the fund created no cause of action against the employer. The lack of employer control of the fund appeared determinative. *Id.* at 289, 39 P.2d at 345-46. Similar cases are discussed *infra* notes 58-59.

36. 129 Ohio St. at 377-78, 195 N.E. at 698 (quoting death benefit certificate).

37. *Id.* at 378, 195 N.E. at 698.

decedent died while in the company's employ, the court reasoned that the certificate was an inducement to the employee to continue working.³⁸ Thus, although Anna Work had no enforceable right during her life, by working until her death she created a binding obligation in favor of her beneficiary.

The court needed no heroic feats of interpretation to eliminate the no-binding-effect clause. It stated instead only that the language "was a part of the contract so far as Anna Work was concerned. She had no right that she could possibly assert, as she had to die before the right would ripen in any one."³⁹ The court apparently viewed the clause as null against the beneficiary, however.⁴⁰ The decision concluded with the proposition that contracts should be upheld and the rights of the parties preserved "if the same can be done without doing violence to language. We find no trouble in upholding this contract."⁴¹

Psutka, the last of the four, adds a somewhat different gloss. The payments at issue were part of a comprehensive non-contributory "pension and death benefit plan" promulgated by the employer that included the following rules applicable to both types of benefits:

"24. This pension plan is a purely voluntary provision for the benefit of employees superannuated or totally incapacitated after long and faithful service, and constitutes no contract and confers no legal rights upon any employee."

"25. Neither the creation of this plan nor any other action at any time taken by the committee shall give to any employee a right to be retained in the service, and all employees remain

38. *Id.* at 379, 195 N.E. at 698. Indeed, ignoring well-established principles of "past consideration," the court even offered that the employer's expression of appreciation for the "duration and faithful character" of Anna Work's services established a further consideration.

39. *Id.*, 195 N.E. at 698.

40. *See Id.* at 380, 195 N.E. at 699 (neither the fact that Anna Work had no obligation to continue her services, nor Mabley & Carew to employ her, "in any wise affected the right of the beneficiary").

41. *Id.*, 195 N.E. at 699. A contemporary writer criticized the court's reasoning as "incompatible with orthodox contract theory," because the disclaimer was so explicit that it negated the possibility that the certificate was an offer. The writer endorsed the result, however, noting the probability of detrimental reliance by the employee, and citing § 90 of the then recently promulgated Restatement of Contracts. The writer concluded that the case demonstrated "a tendency to avoid unconscionable results by the application of more flexible principles." 49 HARV. L. REV. 148, 149 (1935).

subject to discharge to the same extent as if the pension plan had never been created."⁴²

Unlike the courts in *Tilbert*, *Schofield* and *Mabley*, the Supreme Court of Michigan felt constrained to face this problematic language more directly. With only a passing reference to consideration,⁴³ a divided court took up the question of intent. To the majority, the plan consisted of two separate parts: the "positive" promises to pay benefits, and the provisions of rule 24, denying legal effect to the positive promises. If rule 24 were to negate the contractual nature of the plan, then "under the rule that the first of the conflicting clauses in the instrument shall be received and the latter rejected . . . rule 24 must fall."⁴⁴ Unwilling to completely eliminate the offending provision, however, the court compromised by "reading the document as a whole" and "resolving ambiguities against defendant." So viewed, the "reasonable interpretation" was that "the quoted sections were intended to exclude claims of *inchoate* rights under the plan, not to mulct the employees or their dependents of *accrued* death benefits."⁴⁵

The dissent offered a classical analysis, giving primacy to the written expression of intent. From this perspective, it was clear that "[t]here was no intent upon the part of the employers to enter into a binding legal obligation."⁴⁶ The employee's continuation of services "was a recognition that the plan did not constitute a contract nor confer any legal rights upon him."⁴⁷ The result should thus have been simple:

It is a general rule that if the parties to an agreement stipulate that *their* writing, which in all respects appears to be a contract, is not to be a contract, the courts will not enforce it; or if the writing contains stipulations against legal effect, courts will refuse to enforce such writings as contracts.⁴⁸

42. 274 Mich. at 321, 264 N.W. at 387 (quoting pension and death benefit plan).

43. The majority opinion stated only that "ample consideration" existed in the "attraction of more competent workmen to defendant's employ, the inducement of better and more continuous service, and the avoidance of expense of labor turnover." *Id.* at 319, 264 N.W. at 386.

44. *Id.* at 320, 264 N.W. at 386.

45. *Id.*, 264 N.W. at 386 (emphasis in original).

46. *Id.* at 324, 264 N.W. at 388.

47. *Id.*, 264 N.W. at 388.

48. *Id.* at 324, 264 N.W. at 388 (emphasis added). The dissenting opinion, of course, fails to address an obvious factual discrepancy between *Psutka* and the case it

To the dissent, then, the defendant's position was correct: the plan was merely benevolent, and the employer's largesse could be dispensed or withheld, according to its individual determination in each case.

Theoretical considerations aside, it is clear that in an era predating Social Security benefits and statutory protections of vested pension rights, the case-by-case approach suggested by the dissenting justices in *Psutka* was unworkable. One would not expect courts so to expose employees to the whims of their employers.⁴⁹ Indeed, it would be naive to suggest that the results of these cases were in any way unpredictable or extraordinary, either from an historical or doctrinal standpoint.⁵⁰ What is note-

posits: *i.e.*, the only writing in *Psutka* is not "theirs," but that of one party only, offered without any mutual negotiation of terms.

49. On the other hand, Professor Grismore criticized *Psutka* on this very basis. In his view, decisions imposing liability on employers who promulgated voluntary plans acted as a disincentive to their adoption at all. Since he believed that employers would not repudiate such plans absent "compelling financial reasons," he favored reliance upon "moral rather than legal pressure" to ensure their performance until such protections became compulsory. Grismore, *supra* note 29, at 705.

50. While these decisions may have represented questions of first impression in their respective jurisdictions, there was significant authority to the contrary. Possibly the best-known case preceding these was *Meyerson v. New Idea Hosiery Co.*, 217 Ala. 153, 115 So. 94 (1927). There, the employer delivered to the decedent a certificate of group life insurance, accompanied by a form letter provided by the insurance company. While the letter offered assurances to the decedent that the certificate would remain in force "as long as you continue as an employee, without payment on your part or deduction from your salary," it added: "We trust you will accept this certificate in the spirit in which it is given — a genuine expression of good will on our part for your loyal cooperation and service." *Id.* at 156, 115 So. at 96 (emphasis in original). The employer allowed the certificate (as well as additional insurance purchased by the decedent for which deductions were made) to lapse. This was not discovered by the plaintiff until the decedent's death.

The court held for the employer. It saw the group policy as "a voluntary and gratuitous act." Moreover, the employer's agreement to make payments on the additional insurance through payroll deductions was but "a gratuitous agency." The court treated this as a question of consideration. Finding nothing given by the decedent in exchange for the promise, the court concluded that no contract existed. *Id.*, 115 So. at 98.

Meyerson did not involve a no-binding-effect clause as such. The quoted language apparently served only to bolster the court's impression that the employer was acting gratuitously. Even considering that in 1927 promissory estoppel had not yet been extended generally to business and commercial contracts, the decision is puzzling. As Professor Grismore noted in 1936, contemporary courts customarily sought—and found—consideration in the continuation of services. The element of bargain would be inferred from the employer's words: See Grismore, *supra* note 29, at 702-03. *Meyerson's* strict constructionism and lack of concern for obvious equities may be merely a reflection of an era notoriously sympathetic to business interests. See also *Dolge v. Dolge*, 70 A.D. 517, 75 N.Y.S. 386 (1902) (upholding "gratuity" clauses of insurance, endowment, and

worthy is that these decisions consistently de-emphasize the consensual elements of contract liability. An examination of later cases that deal with similar claims strongly reinforces this perception.

A useful sampling can be drawn from Connecticut, where, after *Tilbert*, a well-defined line of cases developed dealing with employee benefits. Such promises have been treated generally as giving rise to binding obligations, despite attempts by employers to make their performance discretionary. Although these cases deal with varying benefits and factual circumstances, the results uniformly suggest the ongoing erosion of the pillar of intent.⁵¹ Only in those cases where the employee's claim had an independent defect, such as failure to comply with stated qualifications,⁵² lack of definiteness,⁵³ or the lack of an enforceable

pension benefit accounts to deny claims of employees of dissolving partnership that claims against the accounts were entitled to priority as wage claims).

51. See *Ellis v. Emhart Mfg. Co.*, 150 Conn. 501, 191 A.2d 546 (1963) (stock option plan was valid contract where employees had to continue employment in order to earn option; employer's attempt to reserve absolute discretion to determine number of shares to which employee was entitled violated public policy against person serving as judge in his own case); *Dolak v. Sullivan*, 145 Conn. 497, 144 A.2d 312 (1958) (attempt to impose succession tax on death benefits contested on grounds that decedent employee did not own accrued benefit; tax levy upheld on grounds that plan amounted to contract that could be extinguished by condition subsequent: the exercise of employer's power of discontinuance, if and to the extent such power existed). Cases from other jurisdictions citing *Tilbert* and consistent with it include *Hoefel v. Atlas Tack Corp.*, 581 F.2d 1 (1st Cir. 1978) (rights to noncontributory pension plan benefits vested once payments began; right to "change, suspend or discontinue" plan inoperative to cut off vested rights); *Novack v. Bilnor Corp.*, 26 A.D.2d 572, 271 N.Y.S.2d 117 (1966) (despite language that act was "voluntary" and created no contractual obligation, board's resolution to pay bonus if employee remained with company constituted unilateral contract, giving rise to debt that could be attached by judgment creditor). See generally *Pineman v. Oechslin*, 494 F. Supp. 525 (D. Conn.), vacated, 637 F.2d 601 (1st Cir. 1980) (summarizing Connecticut law on vesting of pension rights).

52. See *Bird v. Connecticut Power Co.*, 144 Conn. 456, 133 A.2d 894 (1957) (employee's claim for pension denied because resignation after disclosure of malfeasance was deemed voluntary; in dicta, however, the court stated that even where employer reserves absolute discretion over plan, court will interpret plan as a whole to effect general purpose of securing employee loyalty and service; employer cannot defeat employees' reasonable expectations of the promised reward).

53. See *Borden v. Skinner Chuck Co.*, 21 Conn. Supp. 184, 150 A.2d 607 (1958), involving claims for payment of year-end bonuses. The plaintiffs based their claims on (1) the company's past practice of paying bonuses; (2) a company brochure stating that it was "customary" for the company to pay bonuses, subject to the availability of earnings and the discretion of the board; and (3) a reference on a pay slip to voluntary employer contributions for pensions, vacations, holidays, insurance, and bonuses. The court denied recovery, holding that there was no offer and, thus, no contract. The total lack of

promise,⁵⁴ were employers successful in avoiding liability.

Moreover, cases relying upon *Schofield*, *Mabley* and *Psutka* follow similar patterns. Although courts cite various theories of liability, such as vested rights,⁵⁵ unilateral contract,⁵⁶ and reliance,⁵⁷ the decisions almost invariably⁵⁸ indicate a willingness to

certainty regarding the bonus amount was more significant than the employer's language, however. Past payments had varied greatly. *Tilbert* and *Mabley*, both cited by the court, involved payments of a sum certain, or an amount calculable from a sum certain. Faced with a nebulous claim based merely on the fact of prior payments, the court was disinclined to relax its demand for definiteness or to search for the existence of a promise. Lack of definiteness presents an inherent impediment to recovery in bonus cases. See *infra* notes 74-75 and accompanying text.

54. See *Corriveau v. Jenkins Bros.*, 144 Conn. 383, 132 A.2d 67 (1957) (employees' claim for bonus based on contract implied-in-fact failed; mere fact that bonuses had been previously paid gave rise to no present rights).

55. See, e.g., *Siegel v. First Pa. Banking & Trust Co.*, 201 F. Supp. 664 (E.D. Pa. 1961) (noncontributory pension was a vested right, not a gratuity; case remanded to resolve issue of employee's alleged violation of plan provisions); *Luli v. Sun Prod. Corp.*, 60 Ohio St. 2d 144, 398 N.E.2d 553 (1979); *Cantor v. Berkshire Life Ins. Co.*, 171 Ohio St. 405, 171 N.E.2d 518 (1960); cf. *Neuffer v. Bakery & Confectionary Workers Int'l Union of Am.*, 307 F.2d 671, 673-76 (D.C. Cir. 1962) (Burger, J., dissenting) (severance of union member's benefits upheld where, pursuant to contract, union had convicted him of acts against the union; then-Judge Burger argued that benefit had become vested and irrevocable despite discretionary language).

56. See, e.g., *Chinn v. China Nat'l Aviation Corp.*, 138 Cal. App. 2d 98, 291 P.2d 91 (1955) (severance benefits; alternative theory of promissory estoppel); *Cain v. Allen Elec. & Equip. Co.*, 346 Mich. 568, 78 N.W.2d 296 (1956) (severance pay); *Anthony v. Jersey Cent. Power & Light Co.*, 51 N.J. Super. 139, 143 A.2d 762 (1958) (severance pay); *Dangott v. ASG Indus.*, 558 P.2d 379 (Okla. 1976) (severance pay); *Moore v. Postal Telegraph-Cable Co.*, 202 S.C. 225, 24 S.E.2d 361 (1943) (implied duty of good faith); cf. *Ellis v. Victor Elec. Prods.*, 85 Ohio App. 170, 88 N.E.2d 275 (1949) (employee bonus claim; enforceable contract for bonus created where plaintiff accepted pay cut in transfer after being assured that bonus would be "substantially more" than amount of decrease in salary).

57. See *Weesner v. Electric Power Bd.*, 48 Tenn. App. 178, 344 S.W.2d 766 (1961) (vested rights theory also discussed); see also *Chinn v. China Nat'l Aviation Corp.*, 138 Cal. App. 2d 98, 291 P.2d 91 (1955) (alternative grounds on retrial).

58. A well-known case distinguishing *Tilbert* and *Psutka* is *Hughes v. Encyclopedia Britannica*, 1 Ill. App. 2d 514, 117 N.E.2d 880 (1954). There, a class of defendant's employees sought to enforce the defendant's promise to purchase retirement annuities. The defendant reserved the right to "change, amend or discontinue the Plan should future conditions in the judgment of the Company warrant such action;" the plan additionally provided that it was "entirely voluntary on the part of the Company and . . . shall not be construed as creating a contractual relationship between the Company and an eligible employee." *Id.* at 518, 117 N.E.2d at 881. The court denied recovery on both unilateral contract and promissory estoppel theories. The court found no contract because the language of the plan demonstrated that it was voluntary, and expressly denied contractual effect. The estoppel argument was rejected on the grounds that there had been no detrimental change in position, since the plaintiffs had already retired. The court distinguished *Psutka* and *Tilbert* as decisions involving death benefits designed "to

ignore written expressions of intent not to be bound where necessary to avoid a forfeiture of benefits promised before performance, if the benefits are calculable by a reasonably definite standard.⁵⁹ Implicit in these results is the judicial belief that the

avoid the otherwise harsh result of depriving an employee's beneficiary of accrued death benefits." *Id.* at 519, 117 N.E.2d at 882.

Other facts also influenced the court's opinion. First, the employees never had any direct rights against the company for payment. The company's contract with Equitable Life Assurance specified that the benefits would accrue solely to the employees. The plaintiffs were third party beneficiaries with enforceable rights only against Equitable. The court distinguished this situation from cases where the employees' rights were against the employer directly. *See supra* note 35; *see also* cases cited *infra* note 59. Second, all monies paid by the company to purchase annuities remained in the fund, so that the company did not profit by discontinuing the plan. Finally, none of the plaintiffs were receiving benefits when they sued, since each had already retired. In this context, the absence of reliance appears pivotal, although other courts have readily accepted continuing employment as the requisite act of detrimental reliance.

Failure to establish reliance was also determinative in *Armstrong Cork Co. v. Boone*, 30 So. 2d 863 (Miss. 1966), a case distinguishing *Mabley*. While the case was decided on the technical basis of the statute of limitations, the court noted that the promise made after injury to pay disability benefits lacked any element of inducement and was therefore a gratuity, as indicated by language allowing the company to determine the amount of payments.

Two cases citing *Schofield* that denied employee claims, *Genevese v. Martin-Marietta Corp.*, 312 F. Supp. 1186 (E.D. Pa. 1969), and *In re Missouri Pac. R.R.*, 49 F. Supp. 405 (E.D. Mo. 1943), are distinguishable since each involved the employer's discretion to determine compliance with plan requirements rather than the exercise of no-binding-effect clauses.

Perhaps the clearest outright rejection of the reasoning of the principal cases is found in *Umshler v. Umshler*, 332 Ill. App. 494, 76 N.E.2d 231 (1947). Although acknowledging the existence of contrary authority, the court adhered to the gratuity theory of pensions and upheld the no-binding-effect language. Again, however, *Umshler* presented a claim with entirely different equities. The case was a suit for separate maintenance filed by the deserted spouse of the employee in an attempt to obtain payments allegedly due her husband under the plan. Lack of direct inducement or reliance on her part may have influenced the denial of her claim. Perhaps most significant, however, was that the application signed by her husband recited that any allowance was " 'a gratuity which may be discontinued at the pleasure of the company.' " *Id.* at 498, 76 N.E.2d at 233. This acknowledgement introduced an element of apparent mutual assent ordinarily lacking in death benefit and pension cases. *Cf.* discussion *infra* note 71 and accompanying text (dealing with a similar issue in a bonus case). *Umshler* is commonly cited as an example of the generally disavowed gratuity theory of private pensions. *See, e.g.*, Note, *Reappraisal*, *supra* note 18, at 282 n.22.

59. As previously noted, this article does not attempt an exhaustive survey of cases on point. Its methodology is to examine certain paradigmatic cases and to trace the development of their fundamental holdings through subsequent cases with similar issues. Only in this sense is a systematic analysis attempted. Nonetheless, the weight of cases supports this conclusion. Those cases that do not are generally factually distinguishable, although unquestionably some courts have shown greater allegiance to the concept of intent than others.

Other cases outside of the *Tilbert-Psutka* line should be noted. Among well-known

written no-binding-effect clauses did not coincide with the ac-

cases recognizing the contractual nature of private pension plans is *Hurd v. Illinois Bell Tel. Co.*, 234 F.2d 942 (7th Cir. 1956); however, *Hurd* upheld the employer's right to determine within stated guidelines the manner in which pensions would be computed. Cases in which employees have been unsuccessful include *Rochester Corp. v. Rochester*, 450 F.2d 118 (4th Cir. 1971) (clause in pension agreement divesting pension in event of competition by recipient not violative of public policy); *Menke v. Thompson*, 140 F.2d 786 (8th Cir. 1944) (applied gratuity theory of pensions and upheld employer's discretion to determine compliance with conditions of plan in absence of fraud or bad faith); *Gronlund v. Church & Dwight Co.*, 514 F. Supp. 1304 (S.D.N.Y. 1981) (employer's decision not to pay bonus that employee admitted was discretionary was binding unless unreasonable, arbitrary, unfair or capricious, although employee's right to receive severance pay upheld); *Crawford v. Peabody Coal Co.*, 34 Ill. App. 2d 388, 181 N.E.2d 369 (1962) (disabled employee promised pension after he sustained injury provided he not work for another coal company; court held that because he was incapable of working there was no consideration for promise). Clearly, then, employees (or those claiming through them) have fared less well if (1) the issue is compliance with stated prerequisites, rather than changes in the plan itself, or (2) the claimant is one other than the employee or his successor in interest after death. This is not an absolute proposition in either instance, however. See *supra* note 58.

It must be acknowledged that intent still occasionally reigns supreme. See, e.g., *Boase v. Lee Rubber & Tire Corp.*, 437 F.2d 527 (3rd Cir. 1970), applying New York law. Noting that it appeared unclear whether there was binding state court precedent, the court nevertheless held that the employer could, by the use of "clear and unambiguous" language, reserve and exercise the right to terminate a pension plan, even where this deprived retired employees of earned rights. The employer had apparently explicitly disclosed the uncertain nature of the plan to its employees; at least two of the plaintiffs admitted at trial that they had been aware of the termination provision. The court also found *no* countervailing public policy considerations.

Boase was strongly criticized in *Hoefel v. Atlas Tack Corp.*, 581 F.2d 1 (1st Cir. 1978), where it was characterized as an example of the "discredited 'gratuity' theory of pensions." *Id.* at 6. Indeed, intent aside, the *Hoefel* court held that public policy dictated that pension plans be construed to avoid the forfeiture of vested rights. Although *Boase* seems an anachronism, it is possible that the gratuity theory still applies in New York. See Note, *Reappraisal*, *supra* note 18, at 282 n.22.

A more recent example, *Kari v. General Motors Corp.*, 79 Mich. App. 93, 261 N.W.2d 222 (1977), *rev'd per curiam*, 402 Mich. 926, 282 N.W.2d 925 (1978), involved a claim for a "separation allowance." After working for defendant for seventeen years, the plaintiff was granted a six month educational leave in 1972; there was no guarantee of employment upon his return, and when the leave expired, no position was available. Thus, he was "separated" from the company. The plaintiff based his claim on a provision in his employment handbook that "[a] Separation Allowance Plan has been established for the benefit of salaried employees laid off or separated from the payroll under certain circumstances." *Id.* at 95, 261 N.W.2d at 223. The handbook continued, however, that it "is not intended nor is it interpreted to establish a contractual relationship with the employe [sic]." *Id.*, 261 N.W.2d at 223. Moreover, the last page of the handbook included the following italicized disclaimer:

"The contents of this handbook are presented as a matter of information only.

While General Motors believes wholeheartedly in the plans, policies and procedures described here, they are not conditions of employment. General Motors reserves the right to modify, revoke, suspend, terminate, or change any or all such plans, policies, or procedures, in whole or in part, at any time, with or

tual intent of the parties.

This discussion might suggest that employees who can establish reliance on a specific promise of a benefit can presumptively overcome a no-binding-effect clause. That this analysis is over-simplistic is demonstrated by cases involving performance bonuses, which pose superficially similar issues but frequently reach opposite results.⁶⁰

B. Employee Bonuses

One of the modern authorities most frequently cited⁶¹ in support of the freedom not to contract is *Spooner v. Reserve Life Insurance Co.*⁶² The plaintiffs were agents of the defendant insurance company. The defendant issued a bulletin to staff members entitled "Extra Earnings Agreement," reporting the phenomenal growth of the company. In addition to language cheering, challenging, and exhorting its agents, the bulletin stated that each agent "will receive" a bonus based upon his lapse ratio.⁶³ More important, however, was the presence of the

without notice. The language used in this handbook is not intended to create, nor is it to be construed to constitute, a contract between General Motors and any one or all of its employees."

Id., 261 N.W.2d at 223 (quoting employment handbook). While acknowledging that communications to employees may constitute an offer to contract, the court found the above disclaimers too explicit to constitute an offer. In addition, the court found that the manner of communication precluded the possibility of detrimental reliance. In the court's words, "[i]t is difficult to imagine what defendant could have done, short of not mentioning the plan, to prevent the reading of its statement as an offer." *Id.* at 98, 261 N.W.2d at 224. Thus, summary judgment for General Motors was upheld.

The Court of Appeals' opinion in *Kari* indicates that the freedom not to contract is not wholly moribund in employment cases. The plaintiff's claim, however, was somewhat less than compelling. Not only was his initial "severance" voluntary, it was initiated at his request. Moreover, he apparently knew that he might forfeit his job. In light of this, the court was not disposed to find that his continuing employment after promulgation of the plan constituted consideration for a contract; in the court's view, "further negotiations" were necessary. It is questionable whether the court would have reached the same result if the plaintiff had presented a more sympathetic claim, such as an involuntary separation. In any event, the Michigan Supreme Court ultimately reversed the Court of Appeal, and remanded for retrial on the issue of promissory estoppel. *Kari v. General Motors Corp.*, 402 Mich. 926, 282 N.W.2d 925 (1978).

60. See *supra* notes 53-54.

61. E.g., *Kari v. General Motors Corp.*, 79 Mich. App. 93, 98, 261 N.W.2d 222, 224 (1977), *rev'd per curiam*, 402 Mich. 926, 282 N.W.2d 925 (1978); RESTATEMENT (SECOND) OF CONTRACTS § 21, reporter's note to comment b (1979); J. CALAMARI & J. PERILLO, *supra* note 14, § 6-11, at 216 n.98.

62. 47 Wash. 2d 454, 287 P.2d 735 (1955).

63. *Id.* at 456, 287 P.2d at 736. Bonuses would increase in inverse proportion to the

following disclaimer:

“This renewal bonus is a *voluntary contribution* on the part of the Company. It is agreed by you and by us that *it may be withheld*, increased, *decreased* or discontinued, individually or collectively, with or *without notice*. Further, this Renewal Bonus is contingent upon you actually writing business for this Company as a licensed agent at the time such Bonus is paid.”⁶⁴

The bulletin was to be signed by each agent and returned to the home office.

The plaintiffs, who had maintained appropriate lapse ratios, sued when the bonuses described in the bulletin were not paid. Reversing a jury verdict for the plaintiffs, the Supreme Court of Washington held that the above paragraph rendered the promise illusory and unenforceable. It also refused to apply promissory estoppel. While acknowledging that detrimental reliance may sometimes make the gratuitous promises of employers enforceable, the court could find *no* promise, gratuitous or otherwise, in the express language of the bulletin.

The plaintiffs sought to rely upon *Tilbert*, *Mabley*, and *Psutka* to overcome the disclaimer clause.⁶⁵ The court, however, saw the death benefit cases as fundamentally different. In those cases,

in order to avoid seemingly harsh results and to shape the end result a little nearer to the courts' desire, plain language . . . was ignored or so interpreted as to import enforceable promises. No case has been cited to us, nor have we discovered any, in which the right to a bonus has been upheld in a situation in which the employer reserved the right to withhold it.⁶⁶

ratio of lapse of existing policies, according to a specific schedule.

64. *Id.*, 287 P.2d at 737 (quoting “Extra Earnings Agreement” bulletin) (emphasis in original).

65. In addition to the cases, the court mentioned *Schofield* as possible support for the plaintiffs' position. *Id.* at 460, 287 P.2d at 739.

66. *Id.*, 287 P.2d at 739. This statement is puzzling in light of the immediately preceding citation of *George A. Fuller Co. v. Brown*, 15 F.2d 672 (4th Cir. 1926), and *Wellington v. Con P. Curran Printing Co.*, 216 Mo. App. 358, 268 S.W. 396 (1925). In *Fuller*, the plaintiff was given a written promise of a bonus upon his compliance with certain conditions; the employer reserved the power to be the “sole judge as to what bonus, if any, should be paid.” The court held that the plaintiff relied upon a definite promise, thus creating a contract. The court construed the language used by the defendant as limited to the determination of compliance with the stated conditions and the amount of bonus.

The crucial distinction seemed to be that the death benefit cases were brought by named third-party beneficiaries, whereas *Spooner* was prosecuted by the employees themselves. In the court's view, although Reserve Life's acts were "perilously near the perpetration of a fraud,"⁶⁷ the difference in the standing of the plaintiffs justified the court's refusal to "disregard or suppress" the terms of the agreement.⁶⁸

Spooner is, in many ways, an extraordinary case, both in terms of the precedents the court chose not to follow and the inherent equities it elected to ignore. To differentiate it from the death benefit cases because of those cases' supposedly more compelling reliance may have some superficial logic, but the distinction does not withstand analysis. In another sense, the reliance of the claimants in *Spooner* is much more immediate than that of plaintiffs in the death benefit cases. The *Spooner* plaintiffs sought to enforce compensation promised them for their own labors, while the death-benefit beneficiaries had not personally relied on the employers' promises, at least in any identifiable sense. Any "detriment" incurred or reliance manifested was that of their predecessors. Thus, the plaintiffs' claims in *Spooner* would seem, at least, equally forceful.

Further, the *Spooner* court gave no credence to explicit language in the "bulletin" that not only *permitted*, but actively *encouraged*, reliance. The employees were told that the defendant wanted them to "enjoy a sense of real security and see the road of the future stretching clearly ahead"; to "earn more money than [the employees] could anywhere else"; to be "career men—men who are as much concerned about *next year* as *next month*"; to be "very handsomely rewarded" for an "outstanding

The plaintiff in *Wellington* based his claim on a profit-sharing plan that the defendant developed and described in detail in a personal writing to the plaintiff. The plan was characterized as voluntary, and annually renewable. The court held that the plaintiff's performance created a unilateral contract, so that any lack of "mutuality" was irrelevant. Underlying this result was unquestionably a healthy dose of judicial animosity. The plaintiff had become a union organizer at some time after the delivery of the written agreement, and the defendant's refusal to pay was clearly punitive.

While the "no contract" language employed in *Fuller* and *Wellington* is less specific than that in *Spooner*, the *Spooner* court's assertion that no similar bonus cases existed seems unjustified, apart from its artificial reliance on the use of the word "withhold."

67. 47 Wash. 2d at 459, 287 P.2d at 738.

68. *Id.*, 287 P.2d at 738.

job.”⁶⁹ The whole communication was designed as an inducement, and the subordinate nature of the reservation of discretion suggested at most that it would be used in good faith only in extreme instances. In light of the bulletin’s express invitation to rely upon the company’s promises, the court’s decision is particularly difficult to accept.

The opinion barely alluded to the apparent factual basis of the decision: the court’s belief that the plaintiffs were aware of the disclaiming language. Thus, the fact that the plaintiffs were required to sign the “bulletin” and return it to the company may have been pivotal. Even the language of the disclaimer—“[i]t is agreed by you and by us”—couched the plan as a mutually negotiated agreement.⁷⁰ However disingenuous the court’s acceptance of this tactic may have been, it distinguishes the death benefit and pension cases, in which the rights to alter the employer’s obligations were imposed unilaterally. Similarly, *Tilbert*, *Schofield*, *Mabley*, *Psutka*, and their progeny lack the element of written acceptance found in *Spooner*.⁷¹

As previously noted, the *Spooner* result was a departure from many prior employment cases.⁷² Subsequent cases citing

69. *Id.* at 455, 287 P.2d at 736 (emphasis in original). The defendant further stated that by this plan, “the boys are separated from the men. The boys will get no bonus. That Leaves More For The Men.” *Id.* at 456, 287 P.2d at 737 (emphasis in original). Presumably the defendant intended this to apply with equal force to its female agents, since one of the named plaintiffs appears to have been a woman.

70. *Id.* at 456, 287 P.2d at 737 (emphasis in original).

71. *Cf.* RESTATEMENT (SECOND) OF CONTRACTS § 45, comment b (1979) (using *Spooner* as an example of unjustified reliance due to language of “offer”). As previously noted, one pension case, *Umshler*, involved a similar written acceptance, and the claimant likewise was unsuccessful. *See supra* discussion at note 58.

Interestingly, vesting, another theory successful in many death benefit cases, was raised by the plaintiffs to no avail. The court briefly discussed whether the term “withhold” in the disclaimer could refer only to *future* payments, but concluded that it was to be given its ordinary meaning, “to refrain from paying that which is due.” *Spooner*, 47 Wash. 2d at 459, 287 P.2d at 738.

72. *See* *George A. Fuller Co. v. Brown*, 15 F.2d 672 (4th Cir. 1926); *Wellington v. Con P. Curran Printing Co.*, 216 Mo. App. 358, 268 S.W. 396 (1925). *Wellington* is frequently cited as authority for the proposition that continued employment constitutes consideration for the promise of a benefit or bonus. *See* *Lampley v. Celebrity Homes, Inc.*, 42 Colo. App. 359, 594 P.2d 605 (1979); *Nilsson v. Cherokee Candy & Tobacco Co.*, 639 S.W.2d 226 (Mo. Ct. App. 1982); *see also* *Geiwitz v. Geiwitz*, 473 S.W.2d 781 (Mo. Ct. App. 1971) (holding that railroad pension was contract subject to garnishment by divorced wife). *But see* *Molumby v. Shapleigh Hardware Co.*, 395 S.W.2d 221 (Mo. Ct. App. 1965) (employees had no cause of action for noncontributory pension where they had no notice before revocation that pension trust had been established); *Croskey v.*

Spooner have often reached results adverse to employee interests. Yet almost without exception,⁷³ despite language in opinions emphasizing no-binding-effect clauses, other factors appear to determine the outcome. Chief among these is lack of certainty, a recurring problem for plaintiffs in bonus cases.⁷⁴ While employers frequently promise rewards for special efforts, they often fail to quantify a specific benefit. Without explicit guidance on the substance of the promise, many courts have simply denied recovery.⁷⁵ Other courts, however, have demonstrated a willingness to construe contracts to render no-binding-effect clauses inoperative, both in bonus⁷⁶ and other benefit cases,⁷⁷ or to recognize the possibility of recovery based on promissory estoppel.⁷⁸

Kroger Co., 259 S.W.2d 408 (Mo. Ct. App. 1953) (bonus not earned where plaintiff was discharged for sufficient cause).

73. See, e.g., *Albertson v. Ralston Purina Co.*, 586 S.W.2d 776 (Mo. Ct. App. 1979), involving a claim for severance pay. The court held that a policy to pay, "in *limited* and *exceptional* cases, a gratuity to a separated employee" constituted an illusory promise. *Id.* at 777 (emphasis in original). This promise could also have failed for lack of definiteness. See *infra* notes 74-75.

74. In one of the classic cases dealing with lack of certainty, *Varney v. Ditmars*, 217 N.Y. 223, 226, 111 N.E. 822, 823 (1916), the court refused to enforce an employer's promise to pay "a fair share of my profits" as a bonus.

75. See, e.g., *Sandeman v. Sayres*, 50 Wash. 2d 539, 314 P.2d 428 (1957) (no disclaimer, but bonus provision in employment contract merely stated that a "suitable incentive . . . will be decided upon"); *Goodpaster v. Pfizer, Inc.*, 35 Wash. App. 199, 665 P.2d 414 (1983) (employee fired for cause not entitled to bonus where employer retained discretion as to amount); *Calkins v. Boeing Co.*, 8 Wash. App. 347, 506 P.2d 329 (1973) (suggestion bonus; rules referred to amount of cash award, "if any," as totally within the company's discretion). The presence *vel non* of a disclaimer thus seems much less significant than the unwillingness of courts to "make" a contract for the parties. It appears, however, that the presence of a disclaimer may have influenced certain courts to deny alternative claims for recovery in restitution, presumably on the basis that under the circumstances the plaintiff was acting as a volunteer. See RESTATEMENT OF RESTITUTION § 112 (1936); II G. PALMER, THE LAW OF RESTITUTION § 10.1 (1978).

76. See *Osborn v. Boeing Airplane Co.*, 309 F.2d 99 (9th Cir. 1962) (language too uncertain to support summary judgment for employer on basis that it had reserved absolute discretion to appropriate a valuable idea without compensation; both quasi-contract and contract implied-in-fact theories mentioned); *Allen D. Shadron, Inc. v. Cole*, 101 Ariz. 122, 416 P.2d 555 (1966) (court severed language to find alternative promises, with discretionary language only *modifying* the promise to pay a bonus, not rendering it "illusory"; thus employer promised to make a decision—"discretion" was not synonymous with "optional"). In each of these cases, the court ignored obvious problems of uncertainty.

77. See *Hinkeldey v. Cities Serv. Oil Co.*, 470 S.W.2d 494 (Mo. 1971) (claim for severance pay; court construed "management approval" language to apply only to verification of eligibility requirements).

78. *Kari v. General Motors Corp.*, 402 Mich. 926, 282 N.W.2d 925 (1978), *rev'g* 79

Critical analysis of these cases, then, suggests a conclusion similar to that reached as to the pension and death benefit cases: given a statement of commitment by an employer to pay a definite or reasonably calculable monetary benefit, courts have generally endeavored to find a basis to enforce the commitment. The presence of a no-binding-effect clause, disclaimer or reservation of discretion will generally not preclude recovery, so long as the employee has rendered the requested performance, his reliance was reasonable, and his claim is not impaired by extrinsic infirmities. An expression of intent not to be bound appears relevant primarily when it complements another basis for nonenforcement.

Any conclusion regarding the status of the freedom not to contract is premature, however, without examination of a wholly separate category of cases. Letters of intent, which feature no-binding-effect language similar to that utilized in employer-employee cases, add new considerations to the issue of assent.

II. LETTERS OF INTENT

Documents styled "letters of intent" or "memoranda of understanding" are commonly encountered in business transactions.⁷⁹ The use of letters of intent has long been ubiquitous in the securities industry in negotiations for firm commitment underwriting.⁸⁰ They may be used, however, in almost any commercial negotiations, including mergers and other corporate acquisitions,⁸¹ sales of ongoing businesses⁸² and other asset purchases,⁸³ financing and loan agreements,⁸⁴ real estate transactions,⁸⁵ personal property transactions,⁸⁶ and agreements

Mich. App. 93, 261 N.W.2d 222 (1977).

79. See E. FARNSWORTH, *supra* note 14, § 37, at 117 & n.3.

80. C. ISRAELS & G. DUFF, WHEN CORPORATIONS GO PUBLIC 70-71 (1962); Wheat & Blackstone, *Guideposts for a First Public Offering*, 15 BUS. LAW. 539, 553-54 (1960).

81. G. MCCARTHY, ACQUISITIONS AND MERGERS 129-30 (1963); see, e.g., Itek Corp. v. Chicago Aerial Indus., 248 A.2d 625 (Del. 1968).

82. E.g., American Cyanamid Co. v. Elizabeth Arden Sales Corp., 331 F. Supp. 597 (S.D.N.Y. 1971); I.H. Rubenstein & Son v. Sperry & Hutchinson Co., 222 So. 2d 329 (La. Ct. App. 1st Cir.), writ denied, 254 La. 757, 226 So. 2d 521 (1969).

83. E.g., Alaska N. Dev., Inc. v. Alyeska Pipeline Serv. Co., 666 P.2d 33 (Alaska 1983), cert. denied, 464 U.S. 1041 (1984).

84. E.g., Dovenmuehle, Inc. v. K-Way Assocs., 388 F.2d 940 (7th Cir. 1968).

85. E.g., Investment Syndicates, Inc. v. Clark, 3 Wash. App. 1001, 478 P.2d 752 (1970).

86. E.g., Filmvideo Releasing Corp. v. Hastings, 517 F. Supp. 66 (S.D.N.Y. 1981)

relating to entertainment and artistic services and products,⁸⁷ among others.⁸⁸ Although often couched in the form of a mutual commitment, these "agreements" frequently include no-binding-effect clauses.⁸⁹ The reasons for the use of these devices may differ according to the circumstances of each transaction.

In firm commitment underwriting, the use of letters of intent is highly structured. The issuer contemplating a public offering of securities seeks an expression of assurance from the underwriter that it will go forward with the offering, absent some extraordinary occurrence. Without this assurance, the issuer is hesitant to incur the substantial expense of registering the offering with the Securities and Exchange Commission. By the same token, the underwriter is unwilling to undertake a legal obligation at a time when SEC approval is still forthcoming and may not materialize. Thus, the letter of intent constitutes primarily a moral commitment by the underwriter that it will perform *if* the registration statement becomes effective. While the agreement sets forth the general terms of the offering, the underwriter's compensation, and possibly other terms, invariably it will specifically negate the existence of any legal commitment by either party.⁹⁰ This provision is, of course, chiefly for the underwriter's benefit. Nonetheless, since there have been few instances of

(court treated contract of sale as letter of intent).

87. See Taddeo, *Agreeing to Agree: The Importance of Correctly Drafting a Letter of Intent*, N.Y.L.J., April 5, 1985, at 5, col. 1.

88. The precise usage described here is limited to business settings. The question of whether an "agreement" evidences a contractual obligation as opposed to a nonbinding statement of mere intent can, of course, arise in other contexts. See, e.g., *Feick v. Fleener*, 653 F.2d 69 (2d Cir. 1981), discussed *infra* note 99.

89. Obviously, this is not universally true. When the intent not to be bound is unexpressed, writings frequently give rise to "formal contract contemplated" cases. The issue then becomes whether the parties intended to be bound at present, or only upon the execution of a future, more detailed document. For a discussion of these cases, see *supra* note 17 and the authorities cited therein.

90. See authorities cited *supra* note 80. The following is a typical no-binding-effect clause:

This memorandum is accepted by the Company, and by Mr. X on behalf of the selling stockholders, as a statement of mutual intention at this time to effect the proposed transactions along the lines indicated above, but it does not constitute any commitment on the part of the Company, the selling stockholders or any underwriter except as to assumption of expenses as aforesaid. Such a commitment will be undertaken only under the aforementioned underwriting agreement if our customary form shall have been entered into among the Company, the selling stockholders and the underwriters, all acting severally.

C. ISRAELS & G. DUFF, *supra* note 80, at 309.

unjustified default by underwriters,⁹¹ these agreements provide issuers with sufficient comfort to justify the out-of-pocket expenditures that precede the offering.⁹²

In other contexts, letters of intent may be used where intra-corporate or regulatory authorization is a necessary prerequisite to consummation of a transaction. Parties who have not yet completed negotiations on all material terms may use a letter of intent to memorialize the substance of their agreement at its current stage and to provide an impetus to consummate the bargain. Letters of intent may also be useful where other conditions to closing are imposed by either party.

The true letter of intent is, at least to some degree, a mutually negotiated document. This would suggest that in ordinary circumstances, the expression of intent not to contract would go unchallenged. Inevitably, however, a party who renders performance subsequent to the execution of the letter may feel aggrieved if the other party elects to exercise his "freedom" not to proceed. Such circumstances test the extent of the freedom not to contract.

Perhaps the best-known case seeking enforcement of a letter of intent, *Dunhill Securities Corp. v. Microthermal Applications, Inc.*,⁹³ involved securities underwriting, the industry in which the use of such documents is probably the most widely accepted.⁹⁴ Even more interesting is the fact that the underwriter, normally the beneficiary of the no-binding-effect clause and its drafter in this case, brought the action. The plaintiff was to act as principal underwriter for a proposed offering of the defendant's common stock. The parties entered into a letter of intent which provided, in pertinent part:

91. C. ISRAELS & G. DUFF, *supra* note 80, at 70; Wheat & Blackstone, *supra* note 80, at 553.

92. While, at least in theory, the letter of intent has only the sanction of conscience to insure its performance, even the execution of a formal underwriting agreement does not provide absolute assurance to the issuer. Underwriters have long incorporated "market out" provisions allowing them to withdraw from a formal underwriting agreement in the event of sufficiently material adverse developments in the securities markets. See C. ISRAELS & G. DUFF, *supra* note 80, at 78-79; Gourrich, *Investment Banking Methods Prior to and Since the Securities Act of 1933*, 4 LAW & CONTEMP. PROB. 44, 56 (1937); see, e.g., *Blish v. Thompson Automatic Arms Corp.*, 30 Del. Ch. 538, 64 A.2d 581 (1948).

93. 308 F. Supp. 195 (S.D.N.Y. 1969).

94. See *supra* notes 90-92 and accompanying text.

Since this instrument consists only of an expression of our mutual intent, it is expressly understood that no liability or obligation of any nature whatsoever is intended to be created as between any of the parties hereto. This letter is not intended to constitute a binding agreement to consummate the financing outlined herein, nor an agreement to enter into an Underwriting Agreement. . . . In the event that the Underwriting Agreement is not executed and/or the purchase of the securities is not consummated, [the Underwriter] shall not be obligated for any expenses of the Company or for any charges or claims whatsoever arising out of this letter of intent or the proposed financing or otherwise and, similarly, the Company shall not be, in any way, obligated to [the Underwriter].⁹⁵

After approximately two months, during which each party took certain actions pursuant to the letter, the company discovered that the SEC had previously instituted three separate enforcement proceedings against the underwriter. It promptly wrote the underwriter to terminate their relationship.⁹⁶ The underwriter sued to enforce the letter of intent as a binding agreement or, alternatively, to obtain restitution for the value of its services performed and for its out-of-pocket expenditures.

The court rejected both claims. On the contract claim, the opinion quoted Professor Williston: " 'It is indeed true that if the parties to an agreement undertake that no legal obligation shall be created, their undertaking in this regard will be respected by the law, as would any other term of their agreement, provided neither the agreement nor the stipulation itself is illegal.' "⁹⁷ Since there was no ambiguity in their expressions, the court stated that the parties could not be bound unless and until a formal underwriting agreement was executed. The decision emphasized the customary usage of letters of intent in the securities industry, making it clear that such documents are only regarded as *tentative* expressions of intention.

Regarding the quantum meruit claim, the court simply stated that since the underwriter expressly waived compensation in the letter of intent, it could not claim restitutionary relief. Similarly, the plaintiff's knowledge of practices in the securities

95. 308 F. Supp. at 197.

96. *Id.* at 196-97.

97. *Id.* at 197 (quoting 1 S. WILLISTON, *supra* note 5, § 21).

industry relating to registration of public offerings precluded any argument that the underwriter had acted in reliance upon the company's implied request.⁹⁸

Dunhill is strong evidence that the freedom not to contract is still viable.⁹⁹ What remains, however, is to determine its reach. This inquiry should begin with an analysis of *Dunhill* itself. It is, notably, a brief opinion. The court perceived the operative issue in fairly straightforward terms; the language of the decision offers little suggestion of variable factors that might have dictated a contrary result. In addition to expressed intent, two facts appear determinative. The first is that there was little performance prior to the company's letter of termination. Thus, the parties' relationship was still in a fairly executory posture.¹⁰⁰

Even more significant, however, was the industry-wide practice involving letters of intent. Their wide-spread use by securities professionals meant that the underwriter could not seriously allege that it believed the letter to be a binding commitment. Moreover, no disparity in bargaining power was evident. Given the understanding of the nature of such documents in the financial industry, the court might have reached the same result even absent the no-binding-effect clause.¹⁰¹ In either instance, the

98. 308 F. Supp. at 198. The broader question of compensation for performance pursuant to a letter of intent is discussed from the English perspective in Ball, *Work Carried Out in Pursuance of Letters of Intent—Contract or Restitution?*, 99 L.Q. Rev. 572 (1983). The author makes the point that the focus upon intent in cases involving compensation for partial performance based on a letter of intent obscures the operative issue of the extent of legal liability. *Id.* at 586. He argues that restitutionary relief is too limited in many circumstances, and that a flexible approach is needed to protect justified expectations; where appropriate, a hybrid restitution-contract liability should be enforced by the imposition of implied terms. *Id.* at 580, 587-90.

99. Of course, *Dunhill* is not the only evidence, as the previous discussion of *Spooner* illustrates. See *supra* notes 62-71 and accompanying text.

100. This decision supports Professor Atiyah's assertion that classical contract theory's requirement of intent to create legal relations "is concerned with executory agreements alone." The greater the extent of reliance, the more likely a court will use various fictions to "manufacture" the requisite intent. P. ATIYAH, *RISE AND FALL*, *supra* note 12, at 758.

101. A common usage denying the legal effect of certain types of agreements can give rise to a conclusive presumption that all such agreements are unenforceable. For example, English courts have consistently held that collective bargaining agreements are not subject to legal action because of the "climate of opinion" that the parties to such do not intend to be bound. See *Ford Motor Co. v. Amalgamated Union of Eng'g & Foundry Workers*, [1969] 2 Q.B. 303, 331 (bargaining agreements "remain in the realm of undertakings binding in honour"). By statute, these agreements are now conclusively presumed unenforceable absent specific language stating that the parties intend for them to

court would have been justified in finding that reliance upon the letter was unreasonable. Thus, while expressed intent is one operative element in the decision, it is by no means the only salient one.

Subsequent cases citing *Dunhill* have not dealt with the specific issue in that case, that is, the enforceability of an underwriter's letter of intent.¹⁰² Indeed, only one of *Dunhill's* progeny deals with a true letter of intent.¹⁰³ That case, *Garner v. Boyd*,¹⁰⁴

be legally binding. Trade Union & Labour Relations Act, 1974, ch. 52, § 18. See W. ANSON, *supra* note 5, at 66-67; CHESHIRE & FIFOOT'S LAW OF CONTRACT, *supra* note 5, at 104-05; Hepple, *Intention to Create Legal Relations*, 28 CAMBRIDGE L.J. 122, 122-24 (1970).

102. In fact, no case has been found in which a similar attempt has been made.

103. Two cases citing *Dunhill* have characterized the writings at issue as "letters of intent," but neither involved a true no-binding-effect clause. One case, *Feick v. Fleener*, 653 F.2d 69 (2d Cir. 1981), involved a dispute among related heirs over the existence of an agreement to share legal fees stemming from litigation instituted by their decedent and pursued by one group of heirs. The other group elected not to join in the litigation and expressed their unwillingness to make a commitment to share expenses. A letter written by a member of this group suggested, however, that if his interest in the estate were enhanced by the litigation, he would pay his fair share of expenses. The letter expressed a desire to meet and resolve mutual differences on this and other issues affecting the estate. When the litigation proved successful, the other heirs sought to force the writer's group to pay its proportionate share of the legal fees.

In rejecting the claim, the court held that the language of the letter explicitly indicated that the writer intended not to be bound. While the writer stated expressly that he would share in the expenses if he were benefitted, the court saw this in the larger context of an "offer" only to meet and negotiate towards a settlement of many differences. Thus, as in *Dunhill*, there was no "promise" upon which the plaintiffs could rely. Moreover, even if there had been, the plaintiffs could demonstrate no inducement or change in position; they had already bargained for the attorney's services and committed to pay the fee before the letter was written. *Id.* at 79.

The other case, *Filmvideo Releasing Corp. v. Hastings*, 517 F. Supp. 66 (S.D.N.Y. 1981), involved what was in effect a fraudulent transfer. On February 25, 1981, the court had ordered Filmvideo to deliver to Hastings 23 Hopalong Cassidy motion pictures. When Filmvideo failed to comply, Hastings brought an action for contempt. At that point, Filmvideo stated for the first time that it could not comply because it had purportedly sold the pictures to Vanguard Film Corporation on December 14, 1979. The court concluded that the agreement between Filmvideo and Vanguard was a nonbinding letter of intent. In support of this, the court noted that while each had signed the document, it lacked their corporate seals, and used the words "will assign," which showed no present transfer. The court ordered Filmvideo and Vanguard to surrender the films or face a \$10,000 fine. *Id.* at 68.

Presented with Filmvideo's postjudgment story that, two years before litigating property rights to the films, it had sold them to a third party, it is hardly surprising that the court would return Filmvideo and Vanguard to their predealing status. Also noteworthy was that the pictures had been in Vanguard's possession from the outset of the original litigation. (Part of the alleged consideration for the "sale" was Vanguard's cancellation of accrued storage fees. *Id.* at 67.)

serves as an important qualification to the freedom not to contract.

In *Garner*, certain principals of Standard Milling Company, a company in financial distress, organized a second corporation, United's American Milling & Manufacturing Company, for the purpose of acquiring Standard's assets. Those assets were transferred through foreclosure on April 1, 1969, by a deed to United's American, even though United's American's corporate charter was not issued until April 20, 1969. No stock of United's American was ever issued and no new capital was paid into it; it continued Standard's operation with the same assets, properties and personnel. On April 15, 1969, Standard was adjudicated a bankrupt.

In the interim, certain individual defendants signed a letter of intent to exchange United's American's stock for stock in United American Industries, Inc., a separate Arizona corporation. Although this letter was subsequently rescinded, the stock of the Arizona corporation was delivered to the defendants prior to cancellation of the agreement.

Standard's trustee in bankruptcy instituted an action against the individual defendants to obtain possession of the stock of the Arizona corporation. The court found a common scheme by the defendants to transfer the assets of the bankrupt corporation to a new concern in order to defraud the bankrupt's creditors. Employing conflict-of-interest principles, the court reasoned that the defendants, as trustees of the corporation, had unjustly enriched themselves at the expense of the corporation and that the profits they gained were therefore the corporation's property. As successor in interest to the corporation, the trustee was entitled to the stock.¹⁰⁵

In an effort to defeat the trustee's claims, the defendants argued that the agreement with the Arizona corporation was a nonbinding letter of intent that had been rescinded. The court rejected this assertion, stating simply that "[t]he instrument designated as a letter of intent of April 11, 1969 is in reality a

104. 330 F. Supp. 22 (N.D. Tex. 1970), *aff'd per curiam*, 447 F.2d 1373 (5th Cir. 1971).

105. *Id.* at 26-27

contract."¹⁰⁶ Distinguishing the "true letter of intent" in *Dunhill*, the court found that the document included all essential terms of the contract in "clear and unambiguous" language.¹⁰⁷ More significantly, however, those clear and unambiguous promises had been performed, in effect, before rescission.¹⁰⁸ Thus, the "letter of intent" was not merely a memorial of a "preliminary understanding."¹⁰⁹ It was now an executed contract, and the bankrupt, whose assets were the only property traded to the Arizona corporation, was entitled to that contract's benefits.¹¹⁰

The court does not reproduce the language of the April 11 letter, and it is unclear whether it explicitly incorporated a no-binding-effect clause. Had it contained one, it is safe to say that it would not have affected the outcome. Regardless of the common understanding of the effect given to letters of intent, *Garner* makes it clear that such expressions are significant only to an essentially executory agreement. Once one side has rendered substantial performance, parties cannot safely rely upon expressions of intent to effect a return to the status quo ante.¹¹¹ Thus, the freedom not to contract must at least be qualified to this extent: even where a writing may be understood in ordinary usage not to represent a legal obligation, it will acquire increasingly binding characteristics as performance overlaps intention.¹¹² For the drafter who seeks to memorialize a tentative

106. *Id.* at 25.

107. *Id.* at 26.

108. *Id.* The nature of the individual defendants' performance is unclear. The letter provided for the exchange of "the absolute complete ownership of United's American Milling & Manufacturing Co." for 1,733,333 shares in the Arizona corporation. *Id.* at 25. Presumably this referred to a stock exchange, yet no United's American stock was ever issued. It would appear that the Arizona corporation at least assumed control of United's American's operations.

109. *Id.* at 25-26.

110. *Id.*

111. Of course, the element of creditor protection was a powerful impetus to the *Garner* court's refusal to characterize the letter as lacking legal efficacy. However, this does not detract from the ultimate point of the decision: recitals alone are not enough.

112. Similar results might also be reached by arguing that, while the letter of intent is not itself enforceable, subsequent actions of the parties may imply the existence of promises; the letter may then be persuasive evidence of the content of those promises.

An interesting comparison to *Garner* is *I.H. Rubenstein & Son, Inc. v. Sperry & Hutchinson Co.*, 222 So. 2d 329 (La. Ct. App. 1st Cir.), *writ denied*, 254 La. 757, 226 So. 2d 521 (1969), one of the few cases in which the no-binding-effect clause was as explicit as that in *Dunhill*. At issue was a letter of intent concerning the plaintiff's purchase of a

agreement while preserving the flexibility to withdraw in the future, the best alternative is to employ express conditions together with no-binding-effect language.¹¹³

Two recent decisions, however, suggest that even these precautions may be insufficient to insulate the parties from contractual liability. In *American Cyanamid Co. v. Elizabeth Arden Sales Corp.*,¹¹⁴ the defendants, Elizabeth Arden Sales Corporation and the executors of the estate of Elizabeth Arden, entered into a letter agreement with Cyanamid for the sale of the assets and business of the defendant corporation. The letter recited

division of the defendant's business. The letter was signed on March 22, 1968, with closing to occur on March 30. On March 26, defendant notified the plaintiff that it did not intend to go forward. The plaintiff sued for breach, arguing that the letter was a binding sales agreement. The defendant moved to dismiss based upon the letter's last clause:

"It is expressly understood that this is a Letter of Intent and that no liability or obligation of any nature whatsoever is intended to be created between the parties hereto. This letter is not intended to constitute a binding agreement to consummate the transaction outlined herein, nor an agreement to enter into a final agreement. The parties propose to proceed promptly and in good faith to prepare a final agreement providing for the transaction contemplated herein. In the event that such final agreement is not executed, neither party shall have any obligation to the other for expenses or otherwise."

Id. at 330 (quoting Letter of Intent). In upholding dismissal of the plaintiff's action, the court stated that, notwithstanding the thorough detail of the letter of intent, it could not be binding in light of the "plain, clear and unequivocal" language that "the parties did not intend to be bound." *Id.* at 331.

Two additional features of this case should be considered. One is the court's recognition that no-binding-effect clauses are countenanced by the Louisiana Civil Code. *Rubenstein*, 222 So. 2d at 331; see LA. CIV. CODE ANN. arts. 1813-1815 (West 1986). Second, although the closing of the transaction was to take place but a short time after the signing of the letter, defendant rescinded the letter only four days after it was signed. Plaintiff apparently took no action in reliance upon the letter. Under these circumstances no countervailing considerations existed to influence the court to view the letter at other than face value.

113. See *In re Flagstaff Foodservice Corp.*, 25 Bankr. 844 (Bankr. S.D.N.Y. 1982) (letter making offer to purchase, though arguably couched in sufficiently definite terms, was only offer to negotiate where conditioned on board approval, due diligence investigation, and execution of mutually acceptable purchase agreement); cf. *Alaska N. Dev., Inc. v. Alyeska Pipeline Serv. Co.*, 666 P.2d 33 (Alaska 1983) (letter of intent reciting that it was subject to approval of committee could not be supplemented by oral evidence that committee's discretion was limited only to review of price; summary judgment for defendant in breach of contract action affirmed), *cert. denied*, 464 U.S. 1041 (1984). As previously noted, this is the common practice of lenders in loan commitment letters. See *supra* discussion at note 17. *But cf.* *Consolidated Am. Life Ins. Co. v. Covington*, 297 So. 2d 894 (Miss. 1974) (action of insurance company in refusing to make loan for unrelated reasons prevented and excused borrowers from performing necessary conditions; thus loan commitment was binding contract).

114. 331 F. Supp. 597 (S.D.N.Y. 1971).

that consummation was "conditioned upon the execution of a mutually satisfactory purchase agreement and, on the part of Cyanamid, the approval of its board of directors."¹¹⁵ Subsequently the defendants received and accepted a higher offer from Eli Lilly and Company. Thereafter the defendants notified Cyanamid of the sale of the corporation to Lilly. The same day that the notice was received, Cyanamid's board formally ratified the letter agreement and authorized legal action against the defendants.

In analyzing the nature of the letter agreement, the court rejected the defendants' contention that it was a mere "memorandum of understanding." In the court's view, the document contained all of the essential subject matter elements necessary for a contract.¹¹⁶ The problem was instead "mutuality of obligation." Since Cyanamid could not be bound without its board's approval, the letter could obligate neither party until that time.¹¹⁷ This, however, did not mean that the defendants were free to revoke what was otherwise a valid offer. Rather, the court stated that the letter might have constituted an irrevocable offer under New York law.¹¹⁸ If so, formal acceptance by the board of Cyanamid would have created a binding contract. The court believed that a full evidentiary hearing was necessary on this issue. Accordingly, the corporate defendant's motion for summary

115. *Id.* at 602 n.3. Since the letter agreement apparently did not include an explicit no-binding-effect clause, *Elizabeth Arden* may be classified more precisely under the rubric of "formal contract contemplated" cases. See *supra* discussion at note 17.

116. 331 F. Supp. at 603.

117. *Id.* at 605.

118. *Id.* at 605 (citing N.Y. GEN. OBLIG. LAW § 5-1109 (McKinney 1978)). That statute provides in pertinent part as follows:

[W]hen an offer to enter into a contract is made in a writing signed by the offeror, or by his agent, which states that the offer is irrevocable during a period set forth or until a time fixed, the offer shall not be revocable during such period or until such time because of the absence of consideration for the assurance of irrevocability. When such a writing states that the offer is irrevocable but does not state any period or time of irrevocability, it shall be construed to state that the offer is irrevocable for a reasonable time.

This statute, adopted in 1941, served as an analogue to § 2-205 of the Uniform Commercial Code on firm offers. The purpose of each is to substitute the evidentiary function of a signed writing for the traditional requirement of separate consideration for an option contract. Cf. RESTATEMENT (SECOND) OF CONTRACTS § 87 (1979) (offer valid as option contract if in writing and reciting a "purported" consideration). The existence of the New York statute may not have been determinative. A similar result could have been reached based on the implied duty of good faith. See *infra* notes 126-29 and accompanying text.

judgment was denied.¹¹⁹

The second case, *Itek Corp. v. Chicago Aerial Industries*,¹²⁰ moves the letter of intent even further towards the binding end of the continuum between contract and no-contract.¹²¹ The principal stockholders of the defendant, CAI, negotiated an agreement whereby Itek was to purchase all of CAI's assets. Thereafter Itek and CAI executed a letter of intent which provided:

"Itek and CAI shall make every reasonable effort to agree upon and have prepared as quickly as possible a contract providing for the foregoing purchase by Itek and sale by CAI, subject to the approval of CAI stockholders, embodying the above terms and such other terms and conditions as the parties shall agree upon. If the parties fail to agree upon and execute such a contract they shall be under no further obligation to one another."¹²²

While subsequent negotiations were taking place, CAI's principal shareholders renewed discussions with a third party, Bourns, Inc., concerning the purchase of their stock by Bourns. Based upon misrepresentations by these individuals that negotiations with Itek were at an impasse,¹²³ Bourns made a formal offer to purchase their stock on February 25, 1965. The stockholders accepted the next day.¹²⁴ On March 2, CAI notified Itek that negotiations were terminated due to "unforeseen circumstances" and the failure to reach an agreement.¹²⁵ Thereupon, Itek filed suit.

The Supreme Court of Delaware reversed summary judgment in favor of CAI. In response to CAI's reliance upon the non-binding-effect clause, the court stated that all provisions of the paragraph must be considered together, including the undertak-

119. 331 F. Supp. at 606-07. The court dismissed the executors on the grounds that the attempted revocation was solely the act of the corporate defendant, and that the executors were merely acting in what they justifiably viewed as the best interests of the estate in pursuing the higher offer by Eli Lilly. *Id.* at 607.

120. 248 A.2d 625 (Del. 1968).

121. See Knapp, *supra* note 17, at 676.

122. 248 A.2d at 627 (quoting letter of intent).

123. Earlier on the same day that the stockholders made this statement to Bourns, they had met with Itek. At that meeting Itek had acceded to additional terms upon which CAI had insisted. *Id.* at 628.

124. Bourns's offer would have resulted in a return of an additional \$3.00 per share.

125. 248 A.2d at 628.

ing to "make every reasonable effort" to agree upon the terms of a formal contract. This provision obligated each party to attempt in good faith to reach a final and formal agreement. Only if these "best efforts" proved futile would the parties be absolved from further obligations.¹²⁶ Thus, there was sufficient evidence to warrant a finding that both parties intended to be bound, subject to what was in effect a condition subsequent that failure to reach a final agreement after good faith negotiation would discharge them.¹²⁷ Further, the evidence justified the conclusion that CAI had breached its duty to proceed in good faith.¹²⁸

Itek, then, strongly suggests another qualification of the freedom not to contract: one seeking the shelter of a no-binding-effect clause must observe the overriding demands of good faith. The *Itek* court rightly refused to allow artificial recitals of intention to supersede this fundamental duty. Expectations emanating from a promise may take many forms, depending upon its content, while the content may determine in part whether those expectations are justifiable. In all events, however, parties to contracts, or contractual negotiations, are entitled to rely upon the expectation that their counterparts will act according to at least minimum standards of good faith and fair dealing. *Itek* promises that this interest will be protected despite superficial denials of contractual intent.¹²⁹

126. *Id.* at 629.

127. The Second Restatement would characterize this as an event that terminates a duty. RESTATEMENT (SECOND) OF CONTRACTS § 230 (1979).

128. 248 A.2d at 629. The individual stockholders were dismissed on the grounds that no contract could arguably exist between them and *Itek*.

129. The comments to the Second Restatement recognize this implicit limitation on the freedom not to contract. See RESTATEMENT (SECOND) OF CONTRACTS § 21, reporter's note to comment b (1979). For a comprehensive discussion of the question of unjustifiable withdrawal from negotiations, see Knapp, *supra* note 17. Restitution of benefits conferred on the other negotiating party is a further possibility for protecting the interests of parties to letters of intent. The potential for a quantum meruit claim seems obvious, although such arguments have not often arisen in American cases, presumably because of the difficulty of establishing the benefit. See generally Ball, *supra* note 98, at 575-80 (discussing English cases but concluding that restitutionary recovery will ordinarily be too limited to provide adequate protection to the performing party).

III. THE FREEDOM NOT TO CONTRACT AND MODERN CONTRACT LAW

This article posits initially that intent is in retreat as an independent element of contractual liability. The foregoing analysis clearly supports this conclusion, thereby calling into question a fundamental tenet of traditional contract law. The final inquiry of this article asks if other contract theories can better explain these decisions. Certainly the narrow scope of this subject provides no basis upon which to proffer a comprehensive theory of contractual obligation. In the final determination of the scope of the freedom not to contract, however, it is useful to consider how these decisions may fit within the framework of contemporary contract thought. Three alternative theories, reliance, status, and relation, are instructive in this study.¹³⁰

A. Reliance

Among the most dramatic developments in legal theory in this century has been the proliferation of reliance-based liabilities.¹³¹ In contract law, promises rendered enforceable by virtue of promissory estoppel are the most obvious example. The development of the doctrine of promissory estoppel is too well-documented to repeat here.¹³² In cases in which recovery has been granted notwithstanding the presence of a no-binding-effect clause, promissory estoppel has frequently been advanced to explain or justify the result.¹³³ This has particularly been true of

130. In a series of recent articles, Professor Melvin Eisenberg has developed a reconceptualization of contract law that he terms the "responsive model." He argues that contract principles should be based upon two fundamental considerations: fairness, determined by notions of conventional morality, and policy, determined by efficiency and administrability. Thus, the determination of the principles to govern a specific issue should be individualized or standardized, and subjective or objective, depending upon an analysis of that issue in terms of fairness and policy. See Eisenberg, *The Responsive Model of Contract Law*, 36 STAN. L. REV. 1107, 1111 (1984). Because this work is still in its formative stage, no attempt has been made to analyze the subject cases in terms of this model.

131. See P. ATIYAH, *RISE AND FALL*, *supra* note 12, at 771. Professor Atiyah would add to this a belief in the resurgence of benefit-based liabilities, a development that is perhaps more common in England than in America. Ultimately, he views the binding force of promises as flowing from the promise's function as an admission of *other* obligations between the parties, most of which arise from benefits to the promisor or reliance by the promisee. See P. ATIYAH, *PROMISES*, *supra* note 12, at 193-215.

132. For a summary of this topic see Metzger & Phillips, *supra* note 2, at 482-508.

133. See, e.g., J. CALAMARI & J. PERILLO, *supra* note 14, § 6-11, at 216; Metzger & Phillips, *supra* note 2, at 521-22 & n.333.

the employer-employee cases. This analysis is too simplistic, however. To characterize such cases as *Tilbert*, *Schofield*, *Mabley*, and *Psutka* as merely illustrations of the application of the principle of Section 90 of the *Restatement* not only misstates the nature of the doctrine, but ignores a substantial body of similar cases in which clear acts of reliance have *not* been compensated.

In its traditional sense, promissory estoppel has often been characterized as a substitute for consideration. It was the basis for granting relief to one who had relied upon a promise even though the promisor had not sought that reliance.¹³⁴ In the death benefit and pension cases, finding consideration is not a problem. As previously noted, it takes but little judicial imagination to imply a request that the employee continue the faithful performance of his duties in "exchange" for the promise of the future benefit.¹³⁵ This rationalization, however, presupposes the existence of a promise, and that begs the very question at hand. Presumably the purpose of a no-binding-effect clause is the negation of promise, leaving one with *nothing* upon which to rely, reasonably or unreasonably.¹³⁶ At the same time, these clauses frequently have been coupled with other expressions that can only be regarded as inducements to performance. While many opinions employ the catchword "reliance," under traditional analysis the absence or presence of reliance is significant only where one begins with a promise. This is the fundamental element that courts in the foregoing opinions have been forced to supply, ignore, or honor. *Tilbert* and its kin are not, then, "promissory estoppel" cases, although they may be harbingers of a broader, more amorphous species of liability based on reliance alone.¹³⁷

134. See Knapp, *supra* note 10, at 53; Metzger & Phillips, *supra* note 2, at 482-508.

135. Nor, for those inclined to symmetry in such matters, have courts had difficulty in perceiving the benefits enjoyed by employers as the result.

136. See Grismore, *supra* note 29, at 702-03; Metzger & Phillips, *supra* note 2, at 494-98.

137. See G. GILMORE, *supra* note 12, at 66. To Gilmore, this might illustrate one of the areas where contract has been absorbed by tort, with the result that *any* reliance on an assurance must be recompensed. *Id.* at 87-88. Of course, courts have previously applied promissory estoppel to permit recovery in the absence of an enforceable promise. See *Hoffman v. Red Owl Stores*, 26 Wis. 2d 683, 133 N.W.2d 267 (1965) (recovery for reliance expenditures of potential franchisee allowed notwithstanding promise too indefinite to enforce as an offer). Outside of certain specific areas, however, it is arguable that Gilmore overestimates the conquest of contract by tort. See Speidel, *The Borderland of*

A more important determination is *why*, if reliance was the basis for recovery in *Tilbert*, it did not suffice for the plaintiffs in *Spooner* and other bonus cases. Any attempt to distinguish these cases by a qualitative analysis of the nature of the reliance in each is highly questionable.¹³⁸ Moreover, if the reasonableness of reliance is the issue, no clear differences between the two lines emerge. That reliance might be unreasonable due to the nature of the language employed is equally as true in *Tilbert* and its fellows as in *Spooner*. If anything, it is more likely that an employee would rely upon the assurance of a performance bonus than a pension or death benefit because the rewards are much more immediate.

As previously discussed, employees lost many of the bonus cases due to the lack of a definitely promised reward rather than because of the purported reservation of employer discretion;¹³⁹ this is consistent with the traditional requirement in promissory estoppel cases of a specific promise to be enforced. One comes full circle, however, to the lack of a true "promise" in cases like *Tilbert*. Thus, while elements of promissory estoppel may be implicit in certain decisions, it offers no logically consistent explanation for the results achieved throughout the broad spectrum of cases.¹⁴⁰

B. Status

In a well-known article, Professors Childres and Spitz posited that the manner in which courts interpret and enforce contracts often can be explained by the status of the parties.¹⁴¹

Contract, 10 N. KY. L. REV. 163, 196 (1983). See generally Metzger & Phillips, *supra* note 2, at 508-36 (discussing development of promissory estoppel as an independent theory of recovery).

138. See *supra* text accompanying note 73.

139. See *supra* notes 53, 74-75 and accompanying text.

140. Besides *Spooner*, cases in which clear reliance interests of employees went uncompensated include *Boase v. Lee Rubber & Tire Corp.*, 437 F.2d 527 (3d Cir. 1971); *Meyerson v. New Idea Hosiery Co.*, 217 Ala. 153, 115 So. 94 (1927); *Hughes v. Encyclopaedia Britannica*, 1 Ill. App. 2d 514, 117 N.E.2d 880 (1954); *Kari v. General Motors Corp.*, 79 Mich. App. 93, 261 N.W.2d 222 (1977), *rev'd per curiam*, 402 Mich. 926, 282 N.W.2d 925 (1978).

141. Childres & Spitz, *supra* note 11, at 2. The authors' definition of "status" includes both ascribed and achieved status. *Id.* at 2-3 n.5. This distinction is significant. Ascribed status is the status conferred upon a person by such qualities as heredity, age, or maturation. Achieved status is status obtained by a person's own efforts or initiative. See Reh binder, *supra* note 11, at 954.

They suggested that, within certain defined categories of cases, the results should be tested not simply in transactional terms, but according to the status of the parties involved. Taking as their sample cases involving the parol evidence rule, they concluded that an analysis of those cases according to status was more predictive of results than an attempt to apply a unitary parol evidence rule.¹⁴² While this methodology can be applied to the cases discussed in this article, no consistent conclusions emerge.

Childres and Spitz suggested that, for analytical purposes, cases should be divided into three categories. "Formal contracts" include those negotiated fairly and comprehensively between parties with some expertise and business sophistication and of relatively equal bargaining power.¹⁴³ "Informal contracts" are agreements between parties lacking the sophistication usually evident in the business world.¹⁴⁴ "Contracts involving abuse of the bargaining process" is a somewhat nebulous catchall category involving disparity in bargaining power, lack of negotiation, and such obvious examples as adhesion contracts and contracts objectionable on the basis of unconscionability, public policy, fraud, duress, and similar grounds.¹⁴⁵ Most no-binding-effect cases fall within either the first or third categories.

The true "letter of intent" cases would seem to be examples of formal contracts. One would expect that among parties of the same status, courts would be more willing to respect expressions of intent than when dealing with parties of unequal bargaining power. In the ordinary case, sophisticated parties dealing at arm's length could be expected to abide by the rules they impose upon themselves. Only in the event of some superseding flaw in the bargaining process should a court intervene to impose obligations not voluntarily assumed.

The letter of intent cases are in accord with this analysis. *Dunhill* presents no extrinsic reasons for disregarding the parties' expressed intentions.¹⁴⁶ Conversely, *Garner*, *Elizabeth Ar-*

142. Childres & Spitz, *supra* note 11, at 30.

143. *Id.* at 4.

144. *Id.* at 4-5.

145. *Id.* at 5.

146. The same can be said of *I.H. Rubenstein & Son, Inc. v. Sperry & Hutchinson Co.*, 222 So. 2d 329 (La. Ct. App. 1st Cir.), *writ denied*, 254 La. 757, 226 So. 2d 521

den, and *Itek* introduce into the equation fairly blatant elements of bad faith and unfair dealing.¹⁴⁷ There is therefore nothing inconsistent in those courts' willingness to supplement expressions of intent with duties of another sort.

This neat analysis breaks down, however, when one considers the employment cases. These cases presumably would be classified as contract disputes involving abuse of the bargaining process. The pejorative connotations of "abuse" may be misleading. What is meant is that these cases involve, at the very least, disparity in bargaining power and lack of mutual negotiation. One would expect that courts would demonstrate sympathy for employees and seek ways to ameliorate the impact of no-binding-effect clauses. Absent clear indicia that the employee understood and accepted the nonbinding nature of the employer's words, decisions favoring employees would be predictable.

Without repeating what has come before, suffice it to say that courts have offered only fitful support for this conclusion. With no palpable distinctions in the status of the parties, employees have been far more successful in the pension and death benefit cases¹⁴⁸ than in the bonus cases.¹⁴⁹ Each line of cases, however, has been sufficiently inconsistent to suggest that status-based analysis does not yield predictable results.¹⁵⁰

C. *Relational Contracts*

In view of the multitude of scholars whose names are associated with the term, it is difficult to characterize precisely relational theories of contract.¹⁵¹ Professor Ian Macneil, perhaps the preeminent contemporary relationist, uses the term relational contract theory to distinguish the transactional theory that is the basis of traditional contract law.¹⁵² He identifies two fundamental flaws of traditional theory, discreteness and presentia-

(1969), discussed *supra* note 112.

147. See *supra* notes 104-29 and accompanying text.

148. See *supra* notes 20-59 and accompanying text.

149. See *supra* notes 53-54, 62-78 and accompanying text.

150. Death benefit and pension cases in which employees were unsuccessful are discussed *supra* at notes 50, 52, 58-59. Bonus cases in which employees were successful are discussed *supra* at notes 66, 72, 75.

151. For a list of some adherents, see *supra* note 12.

152. See, e.g., Macneil, *Restatement (Second) of Contracts and Presentiation*, 60 VA. L. REV. 589, 592 (1974).

tion. Discreteness is "the separating of a transaction from all else between the participants at the same time and before and after."¹⁵³ Presentation is "the bringing of the future into the present."¹⁵⁴ The transactional model of traditional doctrine, then, fails for two fundamental reasons. First, it ignores the identity of the parties and, thereby, fails to consider any factors outside of their immediate expressions of assent.¹⁵⁵ Second, it attempts to force within those expressions the entire set of rights and obligations between the parties, so that all such matters would be fixed at the time of offer and acceptance.¹⁵⁶ In each instance the goal to be served is the ideal of perfect planning for the future.¹⁵⁷ Since few economic exchanges occur in the discrete transactional pattern, however, the transactional model inevitably proves inadequate.¹⁵⁸ Relationists accordingly seek a new structure based upon relational concepts rather than promise.

Relational theory does not, then, purport to offer a more cogent theoretical basis to explain or rationalize contemporary case law, but seeks to formulate a model by which transactional theory can be reformed to rectify its inconsistencies, inadequacies, and unfairness. This is to be achieved by recognizing relation as the central generating norm of obligations.¹⁵⁹ A critical problem faced by relationists is reconciliation of this norm with the demands of planners and the structural function of intent in defining relations. Relationists recognize that planning is a legitimate, if not primary, goal of contract law.¹⁶⁰ Defining the role of

153. I. MACNEIL, *SOCIAL CONTRACT*, *supra* note 12, at 60.

154. *Id.*

155. *Id.* at 60-62.

156. Macneil, *supra* note 152, at 593.

157. I. MACNEIL, *SOCIAL CONTRACT*, *supra* note 12, at 60.

158. Macneil, *supra* note 152, at 595-96. This inadequacy manifests itself in three primary ways. First, most contemporary contracts are not the products of isolated transactions but rather involve ongoing dealings between the parties. Discreteness tends to bar all such nonpromissory factors from consideration in determining the content of contracts. Second, the transactional theory's obsession with rigid concepts of offer, acceptance, and performance belies the reality that contracts frequently have no neatly identifiable points of demarcation. Finally, presentation attempts to fix all future duties without regard to unanticipated developments occurring after the exchange of promises. Thus, traditional theory must use either fictions or judicial gapfilling to respond to unexpected occurrences. See Lightsey, *supra* note 7, at 49-56.

159. Cf. Feinman, *Critical Approaches to Contract Law*, 30 *UCLA L. REV.* 829, 857 (1983) (characterizing this quest as a somewhat utopian endeavor).

160. See I. MACNEIL, *SOCIAL CONTRACT*, *supra* note 12, at 47; Macneil, *supra* note 2,

intent in the new order presumably dictates a synthesis of relational and transactional principles;¹⁶¹ this challenge is likely to prove the strongest impediment to a workable relational theory. Because the freedom not to contract in its traditional sense is perhaps the ultimate expression of deference to intent, the cases discussed herein pose interesting questions: for example would a relational analysis suggest different results?¹⁶² If so, to the extent that statements of intent are denied primacy, can a relational corollary be articulated which would yield the "right" result in disparate cases? A negative response to this question may indicate that intent and the promise model, although weakened, will probably continue to dominate the foreseeable future of contract law.

In determining the relational response to the freedom not to contract, the initial inquiry concerns the role of consent in the relational scheme. In a broad sense, relationists view expressions of intent as significant primarily to executory contracts of a discrete nature.¹⁶³ When parties instead deal with one another on an ongoing basis, it is the relationship thus established that generates its own set of imperatives. These imperatives, in turn, should principally define the parties' rights and obligations.¹⁶⁴

One would thus expect that at a stage where the parties have as yet had no substantial dealings and their written expressions serve only to define initially their respective obligations, agreed-upon terms should be accorded substantial force. Absent

at 862. Indeed, Macneil has characterized the objective theory of contracts as "a massive effort to harmonize transactional contract law with basic social demands for stability of language." Macneil, *Many Futures*, *supra* note 12, at 812 n.344.

161. *Cf.* Macneil, *supra* note 152, at 605 (discussing the impact of the Second Restatement in effecting this synthesis).

162. In view of the lack of theoretical unity among proponents of relational thought, it should be recognized that any attempt to analyze the subject cases in relational terms is necessarily broad and tentative. Because Professor Macneil has developed what is to date the most coherent statement of relational considerations and objectives, the following discussion draws heavily (although not exclusively) on his work.

163. *See, e.g.*, P. ATIYAH, *RISE AND FALL*, *supra* note 12, at 758; I. MACNEIL, *SOCIAL CONTRACT*, *supra* note 12, at 49-50 (discussing the "triggering role" of intent in contract obligations).

164. *See* P. ATIYAH, *PROMISES*, *supra* note 12, at 193; C. FRIED, *supra* note 9, at 76; L. FULLER, *supra* note 12, at 44 (speaking of "customary" law); Macneil, *Many Futures*, *supra* note 12, at 715-16. Of course, there is no unanimity among relationists regarding *why* relations generate duties, the nature of the obligations thus created, or the exact interaction between relation and promise.

a relationship (in anything beyond the broadest societal sense of the term) which generates mutual imperatives, the parties' expressed intent provides the clearest focus to determine their rights and duties. As the relationship progresses beyond its formative stage, the initial written expression may yield to the internal pressures of the parties' mutual dealings. From this perspective, the letter of intent cases appear entirely consistent. *Dunhill*, which involves only preliminary dealings and industry-wide usages, makes intent preeminent.¹⁶⁵ *Garner*, on the other hand, demonstrates that expressed intent must yield to performance, while *Elizabeth Arden* and *Itek* supplement written expressions of intent with imperatives growing out of duties central to the developing relationship, the justifiable expectation of good faith and fair dealing. In so doing, those courts reach results consonant with prevailing notions of commercial morality.

Again, however, the employment cases present a less logical progression. Relationists have identified employer-employee agreements as among the most obvious examples of contracts peculiarly subject to relational considerations.¹⁶⁶ Both death benefit¹⁶⁷ and bonus cases¹⁶⁸ have been cited to illustrate relation-based duties. Surely this is true in many instances, but the inconsistencies observed in the earlier discussion of these cases conversely illustrate both the strong influence of intent upon our contract system and the difficulties inherent in articulating relational guidelines that amount to anything more than the ad hoc judicial gapfilling so often criticized by relationists.

This problem is apparent in Professor Macneil's discussion of *Tilbert* and *Spooner*. He characterizes both as attempts to

165. The lack of relational imperatives to supplement expressions of intent also may have been determinative in *I.H. Rubenstein & Son, Inc. v. Sperry & Hutchinson Co.*, 222 So. 2d 329 (La. Ct. App. 1st Cir.), writ denied, 254 La. 757, 226 So. 2d 521 (1969), discussed *supra* note 112.

166. See, e.g., L. FULLER, *supra* note 12, at 81; Macneil, *supra* note 152, at 595. Of course, even courts nominally committed to traditional doctrine have long tended to analyze employer-employee contracts in ways that depart from the pristine promise model. See P. ATYAH, *RISE AND FALL*, *supra* note 12, at 764; Childres & Spitz, *supra* note 11, at 2.

167. See Macneil, *supra* note 152, at 600-01; see also *supra* notes 18-60 and accompanying text.

168. See L. FULLER, *supra* note 12, at 81 (discussing bonus cases as "instances where actions—better, interactions—speak louder than words"); see also *supra* notes 62-79 and accompanying text.

shoehorn essentially relational issues into an "unaccommodating format" based on traditional principles of presentation¹⁶⁹—a classic problem of square pegs and round holes. He asserts that in neither case is a black letter rule based on mutual assent and presentation a satisfactory basis for decision.¹⁷⁰ He argues that the manifestations of intent are clearly at odds with the purpose of the employers' promises. He concludes that "[o]nly examination of the relational setting in which the proposals were made reveals principles for determining whether reliance was justified, reliance not primarily on the manifestations of quasi-nonassent but primarily on the relations of which those manifestations were only a small part."¹⁷¹

This analysis is true; unfortunately it does not go far enough, not because it fails to demonstrate that *Tilbert* was decided correctly but because it fails to provide a sufficient rationale for concluding that the *Spooner* court was wrong. Considering the circumstances of each case, in neither were the parties in an executory posture; relationships of some standing were involved. Strong expectations would be generated by those relationships, particularly when an employer who offered with one hand sought to withdraw with the other. In *Tilbert* only a unilateral expression of intent existed to counterbalance these relational considerations; thus, few would quarrel with its result. In *Spooner*, however, one cannot dispense with intent so facilely. As previously noted, the *Spooner* plaintiffs manifested their "assent" to the employer's offer by the classic objective means of signing it.¹⁷² While objective assent has never been equated with subjective understanding, the employees may have been aware of the ephemeral nature of the proposal. If that were true, then two challenges confront the relationists. The first is the possibility that the decision may be justifiable on this basis.¹⁷³ If not, the second challenge is greater still: coherent guidelines must be formulated for determining when assent must yield to relations.

169. Macneil, *supra* note 152, at 600.

170. *Id.* at 601. Macneil speaks of *Tilbert* and *Spooner* in their context as illustrations to sections 21 (formerly 21B) and 45, respectively, of the Second Restatement.

171. *Id.* at 602.

172. See *supra* text accompanying note 71.

173. Even if this were true, the holding was not necessarily correct. Such a rationale may be unduly penal. However, if, as Professor Gilmore has argued, tort has absorbed contract, perhaps those employees might be said to have assumed the risk of their employer's capriciousness.

The articulation of relational objectives and the design of a concomitant structure for decision remain the ultimate impediment for relationists, as indeed to proponents of all alternative contract theories. Both the planning demands of future bargainers and the practical predilections of judges schooled in traditional theory compel the formulation of "rules." Albeit flexible, imbued with a healthy measure of judicial discretion, and subject to the constantly shifting and expanding dictates of good faith, a decisionmaking construct is nonetheless mandated.¹⁷⁴ The inconsistencies of the employment cases and the problem of formulating workable alternative bases for decision demonstrate the problems inherent in practical implementation of alternative models of contract.¹⁷⁵ For the immediate future, and perhaps much longer, the underpinnings of the traditional regime of intent are likely to continue as the fundamental framework of our law of contract, although the continued evolution of contract theory will incorporate increasing recognition of relational factors.¹⁷⁶

IV. CONCLUSION

This article began by questioning the viability of the freedom not to contract incorporated in section 21 of the *Restatement (Second) of Contracts*.¹⁷⁷ An examination of defined categories of cases that invoke the right to exercise this freedom has shown that the *Restatement* formulation is too broad to serve as a predictor of judicial response. To the extent that the freedom not to contract is recognized, it allows bargainers to allocate risks between themselves by opting for a regime of nonenforcement.¹⁷⁸ Commercial parties accordingly may exercise this free-

174. See Feinman, *supra* note 159, at 844, 860; Goetz & Scott, *supra* note 9, at 1322; cf. I. MACNEIL, *SOCIAL CONTRACT*, *supra* note 12, at 86 (recognizing need for discrete legal principles in contract law, but emphasizing that such principles can never be absolute).

175. Professor Macneil acknowledges this difficulty. See Macneil, *supra* note 152, at 605; cf. Feinman, *supra* note 159, at 860 (no alternative theory has been offered that leads inevitably to the correct decision in each case).

176. See Speidel, *supra* note 137, at 196-98 (predicting that courts dealing with complex contract transactions will develop a creative synthesis of contract and tort principles under the general duty of good faith); cf. Blum & Wellman, *supra* note 9, at 937-38 (arguing that mutual assent, as a constitutionally protected liberty, remains the fundamental standard of contract law).

177. See *supra* note 13 and accompanying text.

178. See Goetz & Scott, *supra* note 9, at 1295 & n.73.

dom with a modicum of safety, but only insofar as their actions are consistent with their expressed intent and the accepted practices in their industry. Employers can take little comfort in this freedom, absent some extrinsic defect in their promises that otherwise prevents those statements from constituting "offers," a clear indication of their employees' knowledge of the nonbinding nature of those statements, or the existence of other circumstances that would make reliance unreasonable. Apart from a possible *in terrorem* effect, disclaimers by employers are often only meaningless posturings. The *Second Restatement's* broad formulation of the freedom not to contract is, thus, an outmoded vestige of an era when a written statement of intent reigned supreme without regard to its relation to the actual understanding of the parties.¹⁷⁹ A realistic statement of this freedom must incorporate the qualifications and limitations of reliance, fair dealing, and good faith. The *Second Restatement* should be understood as in need of reform in this area.¹⁸⁰

In light of this evidence of the waning influence of assent, this article has analyzed the implications of several representative cases on the present and future development of contract theory. Perhaps paradoxically, this analysis has demonstrated the enduring predominance of the promise model in judicial reasoning. No satisfactory explanation for the inconsistencies observed in these cases emerges when alternative theories are analyzed. Critical examination dramatically exposes the gaps existing between the abstract statements of those theories and

179. Of course, expressions in contracts that are inconsistent with the reasonable beliefs and expectations of one of the parties are often a hallmark of unconscionability. Courts frequently use that doctrine to address unreasonable provisions. See, e.g., Fort, *Understanding Unconscionability: Defining the Principle*, 9 LOY. U. CHI. L.J. 765, 785-94 (1978).

180. At a minimum, the black-letter rule of the *Second Restatement* should be reworded to state a principle of general application only in commercial transactions. It must be noted that many English authorities seem to accept the freedom not to contract on a fairly uncritical basis. See W. ANSON, *supra* note 5, at 66-69; CHESHIRE & FIFOOT'S LAW OF CONTRACT, *supra* note 5, at 102-04. *But cf.* Hepple, *supra* note 101 (arguing that courts should abandon separate requirement of intention and rest enforceability solely on presence vel non of bargain). It should be noted that the English cases most frequently cited in support of this proposition were decided during the first half of this century. See, e.g., *Rose & Frank Co. v. J.R. Crampton & Bros., Ltd.*, [1925] A.C. 445, *aff'g*, [1923] 2 K.B. 251; *Appleson v. Littlewood, Ltd.*, [1939] 1 All E.R. 464; *Jones v. Vernon's Pools, Ltd.*, [1938] 2 All E.R. 626. Similarly, English courts have not yet embraced the doctrine of promissory estoppel as enthusiastically as their American counterparts. See P. ATIYAH, *RISE AND FALL*, *supra* note 12, at 775-78.

their practical applications by courts. Ultimately cases dealing with this freedom suggest that intent, in a form however modified or circumscribed, will continue for some time as the ground of our law of contract.