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Contracts (1983 Annual Survey of Michigan Law)

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CONTRACTS

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CONTENTS

INTRODUCTION.....	421
I. FORMATION: IMPLIED IN FACT CONTRACTS.....	421
II. PAROL EVIDENCE.....	423
III. INTERPRETATION AND CONSTRUCTION.....	428
IV. DEFENSES: LIMITATION OF ACTIONS.....	430
V. REMEDIES.....	432
A. <i>Rejection under the Uniform Commercial Code</i>	432
B. <i>Rescission for Mutual Mistake</i>	436
C. <i>Damages</i>	438
1. <i>Mental Distress</i>	438
2. <i>Exemplary</i>	440
VI. MEDICAL MALPRACTICE ARBITRATION AGREEMENTS....	441
A. <i>Constitutionality of MMAA</i>	442
B. <i>Unconscionability</i>	444
C. <i>Contracts of Adhesion</i>	444

INTRODUCTION

During the Survey period, the Michigan Supreme Court decided cases involving mutual mistake, the enforceability of a contractual limitation period, and termination of a licensing agreement. The court of appeals considered implied in fact contract theories, interpretation, the parol evidence rule, and claims for exemplary and mental distress damages for breach of contract. In addition, the court of appeals revisited rejection and acceptance under the Uniform Commercial Code, and decided several cases involving medical malpractice arbitration agreements.

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I. FORMATION: IMPLIED IN FACT CONTRACTS

Manifestation of mutual assent by the parties is essential to the making of a contract. When the manifestation emanates from words, the contract is described as "express"; when it is evidenced by conduct, the contract is labeled "implied in fact".¹ The inquiry in each instance is the same: Do the words or actions of the parties demonstrate that the parties have reached an agreement, a common understanding?

In two cases decided during the Survey period, plaintiffs advanced the argument that a governmental entity had breached an implied contract resulting in legally cognizable damages.² In each case, the circuit court granted defendant's motion for summary judgment,³ and the court of appeals affirmed.⁴ Under the principle set forth above, both decisions are clearly correct.

In *Sutton v. Cadillac Area Public Schools*,⁵ plaintiffs argued that voter-approved annexation of three neighboring school districts by the Cadillac Area Public Schools created an implied in fact contract to provide free transportation to and from school for all students living more than one and one-half miles from their school.⁶ In *Gatewood v. City of Detroit*,⁷ the contents of plaintiffs' home were destroyed by a fire that had spread from an adjacent house. A defective fire hydrant, the alleged cause of plaintiffs' loss because of its failure to provide adequate water to fight the fire, was claimed to be a breach of an implied in fact contract that plaintiffs had with the City of Detroit.⁸ The conduct said to create this contractual obligation was supplying water to plaintiffs for residential use.⁹

Regarding *Sutton*, a voter-approved annexation of adjacent school districts patently is not conduct which demonstrates any intent on the part of the annexing school district regarding an obligation to provide free transportation for pupils to and from school. Such a duty might be created by statute,¹⁰ or voluntarily assumed,¹¹ but, it cannot be

1. The legal consequences are the same without regards to which label is attached to the contract. 1 A. CORBIN, CORBIN ON CONTRACTS § 18 (1963).

2. *Gatewood v. City of Detroit*, 121 Mich. App. 57, 329 N.W.2d 34 (1982); *Sutton v. Cadillac Area Pub. Schools*, 117 Mich. App. 38, 323 N.W.2d 582 (1982).

3. 121 Mich. App. at 58, 329 N.W.2d at 34; 117 Mich. App. at 40, 323 N.W.2d at 583.

4. 121 Mich. App. at 60, 329 N.W.2d at 35; 117 Mich. App. at 45, 323 N.W.2d at 585.

5. 117 Mich. App. 38, 323 N.W.2d 582 (1982).

6. *Id.* at 44-45, 323 N.W.2d at 585.

7. 121 Mich. App. 57, 329 N.W.2d 34 (1982).

8. *Id.* at 58, 329 N.W.2d at 34.

9. *Id.* at 58-59, 329 N.W.2d at 34.

10. *See Sutton v. Cadillac Area Pub. Schools*, 117 Mich. App. 38, 44, 323 N.W.2d 582, 585 (1982).

11. *Id.*

said that the school district manifested an intent to undertake that obligation by the act of annexation.

Similarly in *Gatewood*, providing water for residential use for a fee can scarcely be characterized as conduct manifesting an intent by the city to undertake an obligation to provide adequate water for purposes of fighting fires. The question is not whether it would be good public policy to require the city to do so,¹² rather the question is whether it is reasonable for the homeowner to believe that the city has so agreed. Under the circumstances of *Gatewood*, there was only one possible answer.

In both *Sutton* and *Gatewood*, plaintiffs' somewhat far-fetched claims involved an unusual use of the implied in fact contract doctrine. Implied in fact contract cases typically involve a party who has provided goods or services to another party, expecting to be paid therefore, but with no express understanding in that regard. The question presented is whether the conduct of the other party was such that a promise to pay for the goods or services may be inferred.¹³ The claims made in *Sutton*¹⁴ and *Gatewood*¹⁵ arise out of situations far afield from the norm.

II. PAROL EVIDENCE

The parol evidence rule continues to confound Michigan courts. *Goodwin, Inc. v. Orson E. Coe Pontiac, Inc.*¹⁶ and *Union Oil Co. of California v. Newton*,¹⁷ two Michigan Supreme Court cases decided before this Survey period, are the source of much of the confusion; the former for what it says, the latter for what it does not say.¹⁸

The issue in *Goodwin* was whether extrinsic evidence of prior negotiations was admissible for purposes of interpreting the written agreement of the parties.¹⁹ The court discussed the parol evidence rule

12. That question might appropriately be addressed by the legislature. In *Gatewood*, the court of appeals cited *Reinmann v. Monmouth Consol. Water Co.*, 9 N.J. 134, 87 A.2d 325 (1952), as authority for denying plaintiffs' claim. *Reimann*, in fact, involved a claim similar to that in *Gatewood*, but sounding in tort; the reason for the decision was stare decisis. No doubt governmental immunity explains the decision by plaintiffs in *Gatewood* to frame their cause of action in contract.

13. For examples of such cases, see 1 A. CORBIN, CORBIN ON CONTRACTS § 18 (1963). See also RESTATEMENT (SECOND) OF CONTRACTS § 4 (1981) for illustrations.

14. 117 Mich. App. 38, 323 N.W.2d 582 (1982).

15. 121 Mich. App. 57, 329 N.W.2d 34 (1982).

16. 392 Mich. 195, 220 N.W.2d 664 (1974).

17. 397 Mich. 486, 245 N.W.2d 11 (1976).

18. The difficulty with the opinions is not their results—which are clearly correct—but the failure of the court to state clearly and explain the parol evidence rule and its application.

19. 392 Mich. at 198, 220 N.W.2d at 665. A second issue was whether the failure to object at trial to the admission of such evidence precluded consideration of the question on appeal. *Id.*

at length, proffered its own three-pronged test for admissibility of extrinsic evidence,²⁰ and concluded that "[s]ince there was an ambiguity in the contractual language, both the seller and the buyer had the right to introduce parol evidence to clarify its meaning."²¹

In *Newton*, the question was whether extrinsic evidence was admissible to prove that the actual agreement of the parties included terms additional to those embodied in the written expression of their agreement. The court, in a terse per curiam opinion, concluded that the evidence was admissible "[i]f there is no inconsistency" between the proffered evidence and the writing.²²

Before considering these cases further, it is helpful to examine the parol evidence rule. If the parties to a contract intend a writing to be the final and complete expression of their agreement, then neither party can introduce evidence of prior or contemporaneous negotiations or agreements to contradict or even to supplement that writing.²³ This, and this alone, is the parol evidence rule. The concept imbedded therein is not difficult. Indeed, it would seem self-evident: if the parties intend a writing to be the final and complete expression of their agreement, it will be so treated. Evidence of prior negotiations may not be introduced to establish that the agreement is other than that expressed in the writing.

Such evidence is, however, always admissible to: (1) interpret the agreement;²⁴ (2) prove that the writing was a sham, not intended to create legal relations;²⁵ (3) show that the contract is not enforceable because of fraud, illegality, misrepresentation, or mistake;²⁶ or (4)

20. The court stated its test as follows:

- 1) Where ambiguity may exist in a contract, extrinsic evidence is admissible to prove the existence of ambiguity.
- 2) Where ambiguity may exist in a contract, extrinsic evidence is admissible to indicate the actual intent of the parties.
- 3) Where ambiguity exists in a contract, extrinsic evidence is admissible to indicate the actual intent of the parties as an aid in the construction of the contract.

Id. at 209-10, 220 N.W.2d at 671.

21. *Id.* at 219, 220 N.W.2d at 675.

22. 397 Mich. at 488, 245 N.W.2d at 12.

23. *NAG Enter., Inc. v. All State Indus., Inc.*, 85 Mich. App. 194, 198, 270 N.W.2d 738, 740 (1978), *rev'd on other grounds*, 407 Mich. 407, 285 N.W.2d 770 (1979) (citing 3 A. CORBIN, CORBIN ON CONTRACTS § 573 (1963)).

24. 3 A. CORBIN, CORBIN ON CONTRACTS § 579 (1963). *See also* E.A. FARNSWORTH, CONTRACTS § 7.12 (1982).

25. *Tepsich v. Howe Constr. Co.*, 377 Mich. 18, 23-25, 138 N.W.2d 376, 378-79 (1965); 3 A. CORBIN, CORBIN ON CONTRACTS § 577 (1963); E.A. FARNSWORTH, CONTRACTS § 7.4 (1982). During the Survey period, the court of appeals correctly applied this rule in *Harwood v. Randolph Harwood, Inc.*, 124 Mich. App. 137, 333 N.W.2d 609 (1983).

26. *Rood v. Midwest Matrix Mart, Inc.*, 350 Mich. 559, 564-69, 87 N.W.2d 186, 188-90 (1957); 3 A. CORBIN, CORBIN ON CONTRACTS § 580 (1963); E. A. FARNS-

establish the existence of an unfulfilled condition precedent to the effectiveness of the contract.²⁷

Thus, *Goodwin*²⁸ could have been decided with a simple statement that the parol evidence rule does not bar introduction of extrinsic evidence to interpret the agreement of the parties.²⁹ Instead, *Goodwin* linked the admissibility of such evidence to a finding of "ambiguity" in the agreement.³⁰ This was both unnecessary and unfortunate.³¹ The question is not whether a writing appears ambiguous, but what the parties meant by the language they used. All relevant evidence should be admissible to ascertain that intent.³²

In *Newton*, the issue was not interpretation of the written agreement, but whether the parties intended the writing to be the complete and final statement of their agreement. If they did so intend, their writing is a "complete integration," and evidence of prior negotiations is not admissible to contradict or even to supplement the writing.³³ If, on the other hand, the parties intended the writing to be a final statement of the terms contained therein, but not a complete statement of their agreement, then the writing is a "partial integration," and extrinsic evidence may be introduced to supplement but not to contradict the agreement.³⁴

The court in *Newton*, however, failed to present and discuss the issue in this manner. It stated that the "question is whether the proffered parol evidence is inconsistent with the written language."³⁵ In so stating, the court must implicitly have concluded that the writing was

WORTH, CONTRACTS § 7.4 (1982). This issue arose during the Survey period, and the court of appeals properly decided it in *Gonman v. Soble*, 120 Mich. App. 831, 328 N.W. 2d 119 (1982).

27. 3 A. CORBIN, CORBIN ON CONTRACTS §§ 577, 589 (1963); E. A. FARNSWORTH, CONTRACTS § 7.4 (1982).

28. 392 Mich. 195, 220 N.W.2d 664 (1974).

29. See *supra* note 24.

30. 392 Mich. at 209-10, 220 N.W.2d at 671. See *supra* note 21.

31. For an example of the unworkability of the ambiguity test see *Union Oil Co. of California v. Newton*, 397 Mich. 486, 245 N.W.2d 11 (1976). Relying on *Goodwin, Inc. v. Orson E. Coe Pontiac, Inc.*, 392 Mich. 195, 220 N.W.2d 664 (1974), the trial court and the court of appeals, in deciding whether extrinsic evidence was admissible, used the ambiguity test. The trial court concluded that the writing was ambiguous, and, therefore, extrinsic evidence was admissible. The court of appeals' conclusion was to the contrary; thus, extrinsic evidence was not admissible.

32. The court in *Goodwin* correctly stated that the "cardinal rule in the interpretation of contracts is to ascertain the intention of the parties." 392 Mich. at 209, 220 N.W.2d at 671. The court then, unfortunately, proposed its ambiguity test. *Id.* See *supra* note 20.

33. RESTATEMENT (SECOND) OF CONTRACTS § 215 (1981); 3 A. CORBIN, CORBIN ON CONTRACTS § 582 (1963).

34. RESTATEMENT (SECOND) OF CONTRACTS §§ 210(2), 215, 216 (1981); 3 A. CORBIN, CORBIN ON CONTRACTS § 581 (1963).

35. 397 Mich. at 488, 245 N.W.2d at 12.

a partial, not a complete, integration; otherwise, whether the extrinsic evidence is consistent with the writing is of no concern. Unfortunately, the court did not provide any guidance on the troublesome matter of determining whether a writing is a complete or partial integration. To this day, the courts remain inconsistent in their selection of a method for making this determination,³⁶ a fact neatly illustrated by three cases decided by the court of appeals during this Survey period.

In *In re Bluestone Estate*,³⁷ decedent had personally agreed to guarantee certain financial obligations taken on by a restaurant of which he was an officer. After decedent's death, the restaurant filed for bankruptcy, and creditors asserted claims against decedent's estate to enforce the written guarantees. The probate court found that the language of the guarantees was unambiguous, thus precluding the estate from introducing parol evidence to show certain unfulfilled conditions precedent to the enforceability of the agreements.³⁸ The court of appeals agreed, citing *Goodwin*.³⁹

Bluestone can be criticized for endorsing and applying the *Goodwin* ambiguity test. Parol evidence is always admissible to show that the contract was subject to an unfulfilled condition precedent to its effectiveness.⁴⁰ The result in *Bluestone*, however, appears to be correct. Despite its conclusion that the writing was unambiguous, the probate court apparently afforded decedent's estate an opportunity to produce evidence of a condition precedent, but the estate failed to do so.⁴¹

In *In re Chiodo Estate*,⁴² the court of appeals concluded that a check with the handwritten notation "labor" on it was not a complete integration; parol evidence was, therefore, admissible to establish an oral contract.⁴³ The court did not use the ambiguity test of *Goodwin*,

36. See *Michigan Nat'l Bank of Detroit v. Holland-Dozier-Holland Sound Studios*, 73 Mich. App. 12, 250 N.W.2d 532 (1976), where the court of appeals, presuming that "the Supreme Court's most recent utterance" controlled, followed the *Newton* inconsistency doctrine. *Id.* at 16, 250 N.W.2d at 534. See also, *NAG Enter., Inc. v. All State Indus., Inc.*, 85 Mich. App. 194, 270 N.W.2d 738 (1978), *rev'd on other grounds*, 407 Mich. 407, 285 N.W.2d 770 (1979); *Oakland County v. City of Detroit*, 81 Mich. App. 308, 265 N.W.2d 130 (1978).

In *NAG Enterprises*, the court stated that "*Newton* is in accord with pre-*Goodwin* cases which use the inconsistency—opposed to the ambiguity—language." 85 Mich. App. at 199-200, 270 N.W.2d at 741. On appeal, the supreme court merely reported the lower court's intention to follow *Newton*, and reversed the case on other grounds. 407 Mich. 407, 410, 285 N.W.2d 770, 771 (1979).

37. 121 Mich. App. 659, 329 N.W.2d 446 (1982).

38. *Id.* at 664, 329 N.W.2d at 449.

39. *Id.* at 665, 329 N.W.2d at 449.

40. See *supra* note 27.

41. 121 Mich. App. at 666, 329 N.W.2d at 449.

42. 123 Mich. App. 254, 333 N.W.2d 241 (1983).

43. *Id.* at 256-57, 333 N.W.2d at 242.

nor did it apply the inconsistency test of *Newton*. Instead, relying on an 1893 Michigan case,⁴⁴ the court adopted the much-discredited⁴⁵ four-corners test for determining whether a writing is a complete or partial integration. The court stated:

The test of the completeness of the writing proposed as a contract is the writing itself. If this bears evidence of careful preparation, of a deliberate regard for the many questions which would naturally arise out of the subject-matter of the contract, and if it is reasonable to conclude from it that the parties have therein expressed their final intentions in regard to the matters within the scope of the writing, then it will be deemed a complete and unalterable exposition of such intentions. If, on the other hand, the writing shows its informality on its face, there will be no presumption that it contains all the terms of the contract. In every case, therefore, the writing must be critically examined in the light of its surrounding circumstances, with a view of determining whether it is a memorial of the transaction.⁴⁶

Finally, in *Vergote v. K Mart Corp.*,⁴⁷ seller agreed to sell land, which was to be the site for a new shopping center, and buyer, among other things, agreed to construct access roads to seller's remaining property and dedicate them to public use. This agreement was included in the initial purchase offer.⁴⁸ The purchase offer was later amended, and buyer's obligation regarding the access roads was expressly eliminated.⁴⁹

The seller contended that buyer gave seller verbal assurances that the access roads would be constructed and dedicated. When buyer failed to do this, seller sued. At trial, buyer raised the parol evidence rule, arguing that the court could not admit extrinsic evidence since the written agreement unambiguously stated that buyer had no obligation to construct and dedicate the roads. The trial court agreed, and granted buyer's motion for summary judgment.⁵⁰ The court of

44. *Butler v. Iron Cliffs Co.*, 96 Mich. 70, 55 N.W. 670 (1893).

45. 3 A. CORBIN, CORBIN ON CONTRACTS §§ 581, 582 (1963); RESTATEMENT (SECOND) OF CONTRACTS § 210, Comment b (1981); E.A. FARNSWORTH, CONTRACTS § 7.3 (1982).

46. 123 Mich. App. at 257, 333 N.W.2d at 242 (quoting *Butler v. Iron Cliffs Co.*, 96 Mich. at 78, 55 N.W. at 673 (1893)).

47. 125 Mich. App. 48, 336 N.W.2d 229, *leave to appeal denied*, 417 Mich. 1100.39 (1983).

48. *Id.* at 49-50, 336 N.W.2d at 229.

49. *Id.* at 50-51, 336 N.W.2d at 230.

50. *Id.* at 51, 336 N.W.2d at 230.

appeals reversed.⁵¹

As in *Chiodo*⁵² and *Newton*,⁵³ the question in *Vergote* was whether the written expression of the agreement was a complete or partial integration. The *Vergote* court properly held that the question turned on the intent of the parties, and that all evidence relevant to the determination of that intent was admissible, including "evidence of prior or contemporaneous agreements or negotiations."⁵⁴

The court in *Vergote* correctly eschewed the ambiguity and the four-corners tests.⁵⁵ Both tests suffer from an undue and arbitrary limitation on proof. If the intent of the parties is at issue, it is difficult to see why the introduction of relevant evidence is precluded simply because the document does not seem ambiguous or appears complete within its four-corners. The test adopted by *Vergote* avoids the strictures imposed by the other tests. Under it, a party is permitted to establish by whatever proof is available that the writing does not express the complete understanding of the parties and is, therefore, subject to modification.

III. INTERPRETATION AND CONSTRUCTION

Two cases presenting issues of contract interpretation⁵⁶ were decided during the Survey period.⁵⁷ One involved termination of an employment contract;⁵⁸ the other termination of a licensing agreement.⁵⁹

The issue in *Stroud v. Glover*⁶⁰ was whether the term "upon notice" in an employment contract meant that the contract could be terminated immediately after notice was given or only after notice

51. *Id.* at 53, 336 N.W.2d at 231.

52. 123 Mich. App. 254, 333 N.W.2d 241 (1983).

53. 397 Mich. 486, 245 N.W.2d 11 (1976).

54. 125 Mich. App. at 52, 336 N.W.2d at 231.

55. The court did not cite either *Goodwin, Inc. v. Orson E. Coe Pontiac, Inc.*, 392 Mich. 195, 220 N.W.2d 664 (1974) or *Union Oil Co. of California v. Newton*, 397 Mich. 486, 245 N.W.2d 11 (1976). The only authority relied on was *NAG Enter., Inc. v. All State Indus., Inc.*, 85 Mich. App. 194, 270 N.W.2d 738 (1978), *rev'd on other grounds*, 407 Mich. 407, 285 N.W.2d 770 (1979), which adopted the test proposed by Professor Corbin. See 3 A. CORBIN, CORBIN ON CONTRACTS § 573 (1963).

56. Technically, "interpretation" of a contract involves ascertaining the intent of the parties regarding the meaning of the language or words of their contract, and "construction" of a contract involves determining its legal effect. The terms are often, however, used interchangeably. See 3 A. CORBIN, CORBIN ON CONTRACTS § 534 (1963).

57. Several cases presenting issues of interpretation of insurance contracts were decided during the Survey period. Those cases are discussed in Baker & Samper, *Insurance Law*, 30 WAYNE L. REV. 675 (1984), and will not be addressed here.

58. *Stroud v. Glover*, 120 Mich. App. 258, 327 N.W.2d 462 (1982).

59. *Lichnovsky v. Ziebart Int'l Corp.*, 414 Mich. 228, 324 N.W.2d 732 (1982).

60. 120 Mich. App. 258, 327 N.W.2d 462 (1982).

followed by a reasonable time. The plaintiff, a saleswoman for defendant real estate broker, sued for breach of contract alleging that the contract had been terminated without the requisite notice and reasonable time.⁶¹

The court of appeals, noting that the term "upon" had various meanings,⁶² affirmed the circuit court's decision, which had affirmed, as not clearly erroneous, the trial court's conclusion that termination of the contract required both prior notice and a reasonable time.⁶³ The court reasoned that this interpretation was in accord with the parties' intent.⁶⁴

Generally, when an agreement contains no provision for its duration or term, it is considered a contract for an indefinite term, terminable at the will of either party.⁶⁵ The supreme court concluded, however, in *Lichnovsky v. Ziebart International Corp.*,⁶⁶ that this rule "does not apply where the agreement, although of uncertain duration, contains a provision specifying the manner of termination."⁶⁷

61. *Id.* at 261-62, 327 N.W.2d at 464.

62. The court, citing *Sanford v. Luce*, 245 Iowa 74, 60 N.W.2d 885 (1953), stated that the word "upon" is elastic in meaning and, depending on its context, could mean "as soon as," "at the time of," or "after." 120 Mich. App. at 262, 327 N.W.2d at 464.

63. 120 Mich. App. at 262-63, 327 N.W.2d at 464.

64. The court stated:

Where a contract is open to construction, it is the duty of the court to determine if possible the true intent of the parties. In determining true intent, a court should consider the language employed in the contract, its subject matter, and the circumstances surrounding the making of the agreement.

Id. at 262, 327 N.W.2d at 464.

In *Hoch v. Hitchens*, 122 Mich. App. 142, 322 N.W.2d 440 (1982), the court examined the parties' conduct to interpret their agreement. *Hoch* involved a land contract which provided for monthly installment payments due on the fourteenth of each month. Before the payment in issue, buyer had consistently mailed payments on or before the fourteenth, and seller had readily accepted them after that date. In reversing the trial court's order of foreclosure, which had been based on a receipt of payment by seller after the fourteenth, the court stated:

It is well settled that, in contractual relationships, the actual delivery of legal tender is not required where there is a course of dealing which justifies the debtor in believing that some other means (*e.g.*, mailing) and forms of tender (*e.g.*, personal check) will suffice (citation omitted). The risk of loss or delay in delivery of a payment made by mail must be borne by the creditor who has agreed to accept payments by mail, not the debtor.

Id. at 147, 322 N.W.2d at 442.

65. See *O'Connor v. Hayes Body Corp.*, 258 Mich. 280, 242 N.W. 233 (1932). See also *Holt v. St. Louis Union Trust Co.*, 52 F.2d 1068 (4th Cir. 1931); *Adkisson v. Ozment*, 55 Ill. App. 3d 108, 370 N.E.2d 594 (1977); *Paisley v. Lucas*, 346 Mo. 827, 143 S.W.2d 262 (1940).

66. 414 Mich. 228, 324 N.W.2d 732 (1982).

67. *Id.* at 236, 324 N.W.2d at 737. The provision at issue stated in relevant part:

The parties entered into a licensing agreement for the operation of rustproofing stations. The defendant sought to terminate that agreement, arguing that since it was for an indefinite duration, it was terminable at will upon reasonable notice.⁶⁸ Plaintiff argued that the license was terminable after proper notice only in the event of default and the plaintiff's failure to cure.⁶⁹ Invoking generally accepted rules of interpretation,⁷⁰ the court concluded that the elaborate termination process outlined in the agreement indicated the parties' intent to require cause for termination despite the fact that the agreement was for an indefinite term.⁷¹

IV. DEFENSES: LIMITATION OF ACTIONS

Given the decision of the Michigan Supreme Court in *Camelot Excavating Co. v. St. Paul Fire and Marine Insurance Co.*,⁷² the result in *Armand v. Territorial Construction, Inc.*,⁷³ was predictable. In *Camelot*, the court held that the one-year limitation period in a labor and materials payment bond, rather than the general six-year provi-

10. This license agreement shall be *in full force and effect indefinitely, unless terminated at an earlier date in accordance with the provisions of paragraph 11.*

11. Should licensee fail to perform any of the terms, conditions or provisions of this license agreement, and shall remain in default for a period of 30 days after the receipt of a notice by licensor by registered letter *setting forth the reasons and grounds for default*, licensor shall thereafter have the right to terminate this agreement forthwith by registered letter to licensee (emphasis added).

Id. at 235 n.12, 324 N.W.2d at 736 n.12.

68. *Id.* at 235, 324 N.W.2d at 736.

69. *Id.* at 236, 324 N.W.2d at 736.

70. In the case of ambiguity, interpretation of an agreement will be made against the drafter. In this case, however, the defendant's predecessor had drafted the agreement. See *Ladd v. Teichman*, 359 Mich. 587, 103 N.W.2d 338 (1960); *Bonney v. Citizens' Mut. Auto. Ins. Co.*, 333 Mich. 435, 53 N.W.2d 321 (1952). The "cardinal" rule, however, is to ascertain the parties' intention. "To this rule all others subordinate." *McIntosh v. Groomes*, 227 Mich. 215, 218, 198 N.W. 954, 955 (1924). See also *Goodwin, Inc. v. Orson E. Coe Pontiac, Inc.* 392 Mich. 195, 220 N.W.2d 664 (1974).

71. 414 Mich. at 243, 324 N.W.2d at 740. The supreme court granted leave to appeal specifically to steer the court of appeals away from adopting the "Missouri Rule." *Id.* at 245-46, 324 N.W.2d at 741. The "Missouri Rule" states that:

in agreements for an unspecified duration the principal's otherwise unfettered right to terminate the arrangement at will is limited by the agent's right to enforce the agreement for such time as will afford him a reasonable opportunity to recoup the expenses he has incurred in preparing to perform his obligations.

93 Mich. App. 60, 72, 285 N.W.2d 795, 801 (1979).

72. 410 Mich. 118, 301 N.W.2d 275 (1981).

73. 414 Mich. 21, 322 N.W.2d 924 (1982).

sion of the statute of limitations,⁷⁴ applied against a subcontractor, third-party beneficiary of the contract, in a cause of action brought against the surety.⁷⁵

The payment and materials bond at issue in *Armand* contained a similar one-year limitation. In addition, a provision in the bond precluded suit by a subcontractor for ninety days after last furnishing labor or materials. The *Armand* court concluded that the ninety day waiting period did not toll the one-year limitation period,⁷⁶ and then held that the actual limitation period provided by this contract—nine months—was enforceable.⁷⁷

A contractual period of limitation will be upheld, even though it is shorter than the applicable provision of the statute of limitations, if it is reasonable.⁷⁸ The fact that the subcontractor in *Camelot*, who had not been a party to the surety contract, did not know of the shorter limitation period was not fatal. Reasonableness requires only “that the claimant have sufficient opportunity to investigate and file an action, that the time not be so short as to work a practical abrogation of the right of action, and the action not be barred before the loss or damage can be ascertained.”⁷⁹ The *Camelot* court concluded that with reasonable diligence the subcontractor could have ascertained the one-year period of limitation and protected its rights under the bond.⁸⁰ Similarly, in *Armand*, the court concluded that the nine-month limitation period was reasonable: “This was ample time during which [the subcontractor] could have filed suit and protected its contractual rights.”⁸¹

While *Armand* does go one step beyond *Camelot*, the difficult question in these cases was the one that the *Camelot* court resolved against the subcontractor. Once the court was willing to enforce a period of limitation contractually shortened to one year in a contract of adhesion against a third-party beneficiary, enforcement of such a

74. MICH. COMP. LAWS ANN. §§ 600.5807(8), .5813 (1968).

75. 410 Mich. at 125, 301 N.W.2d at 276.

76. 414 Mich. at 22, 322 N.W.2d at 924.

77. *Id.* at 27-28, 322 N.W.2d at 927.

78. 410 Mich. at 126, 301 N.W.2d at 277 (citing *The Tom Thomas Org., Inc. v. Reliance Ins. Co.*, 396 Mich. 588, 242 N.W.2d 396 (1976)). The court in *The Tom Thomas* case did not have to decide the issue of the enforceability of the one-year limitation period in an inland marine insurance policy. The court concluded that the insured had timely commenced its cause of action within the one year period. 396 Mich. at 597, 242 N.W.2d at 400.

79. 410 Mich. at 127, 301 N.W.2d at 277.

80. *Id.* at 137, 301 N.W.2d at 282.

81. 414 Mich. at 27, 322 N.W.2d at 927. The nine-month limitation period was the result of the one-year limitation period provided for in the contract less the ninety days that claimants had to wait after last furnishing labor or materials before suing on the bond. *Id.* at 22-23, 322 N.W.2d at 924-25.

period shortened by an additional ninety days is not startling.⁸²

V. REMEDIES

A. *Rejection under the Uniform Commercial Code*

In *Colonial Dodge, Inc. v. Miller (On Rehearing)*,⁸³ the Michigan Court of Appeals addressed the issues of acceptance and rejection of non-conforming goods under the Uniform Commercial Code (the Code), and reversed, without mention, its earlier decision in the same case.⁸⁴ The statements of facts in the two opinions are not entirely consistent. Buyer picked up a new car at seller's dealership, drove it a short distance, and exchanged cars with his wife who drove it home. After working the night shift, buyer returned home and was informed by his wife that the car had no spare tire. The dealership was closed, so buyer waited until the next morning to call. He spoke to the salesman who sold him the car and either was told that the car had no spare tire because of a tire strike,⁸⁵ or was offered no explanation for the missing spare tire.⁸⁶ Not satisfied, buyer told the salesman to pick up the car since he no longer wanted it, and that he was going to stop payment on his checks. Buyer then parked the car in front of his house and refused receipt of the license plates. When the temporary vehicle registration expired, the car was towed away by the police.⁸⁷

Seller sued for the purchase price, claiming that buyer had accepted the car.⁸⁸ The trial court agreed that buyer had accepted, but awarded seller the contract price less the resale value of the car.⁸⁹ Seller appealed. The court of appeals originally reversed and remanded, holding that the trial court's finding that defendant had accepted the car was "clearly erroneous."⁹⁰ On rehearing, the court

82. Justice Levin wrote a concurring opinion in *Camelot* to emphasize that the decision is limited to cases involving subcontractors as third-party beneficiaries of a labor and materials payment bond. 410 Mich. at 140-43, 301 N.W.2d at 284. Whether or not the court holds the line suggested by Justice Levin, *Armand* is clearly within a narrow reading of *Camelot*.

83. 121 Mich. App. 466, 328 N.W.2d 678 (1982) (on rehearing) (leave to appeal pending).

84. *Colonial Dodge, Inc. v. Miller*, 116 Mich. App. 78, 322 N.W.2d 549 (1982).

85. 116 Mich. App. at 81, 322 N.W.2d at 550.

86. 121 Mich. App. at 471, 328 N.W.2d at 679.

87. *Id.* at 471-72, 328 N.W.2d at 679; 116 Mich. App. at 81-82, 322 N.W.2d at 550-51.

88. 116 Mich. App. at 82, 322 N.W.2d at 551. MICH. COMP. LAWS ANN. § 440.2607 (1967) provides in pertinent part: "(1) The buyer must pay at the contract rate for any goods accepted."

89. 116 Mich. App. at 82, 322 N.W.2d at 551.

90. *Id.* at 85, 322 N.W.2d at 552.

reached the opposite conclusion and affirmed the finding of the trial court that buyer had accepted the car because the parties at trial had so agreed.⁹¹ The dissent stated that there was nothing in the record to support such a finding.⁹²

Acceptance is a term of art.⁹³ The court of appeals correctly stated in its first opinion that mere possession of goods does not constitute acceptance.⁹⁴ Buyer is permitted a "reasonable opportunity to inspect" goods before buyer is deemed to have accepted them.⁹⁵ The court of appeals initially found, without discussion or analysis, and contrary to the conclusion of the trial court, that buyer in the instant case did not have a reasonable opportunity to inspect the car.⁹⁶ The court also found, again without explanation, that buyer's actions regarding the

91. 121 Mich. App. at 472-74, 328 N.W.2d at 679-80.

92. *Id.* at 478, 328 N.W.2d at 682 (Deming, J., dissenting).

93. MICH. COMP. LAWS ANN. § 440.2606 (1967) provides:

- (1) Acceptance of goods occurs when the buyer
 - (a) after a reasonable opportunity to inspect the goods signifies to the seller that the goods are conforming or that he will take or retain them in spite of their nonconformity; or
 - (b) fails to make an effective rejection (subsection (1) of section 2602), but such acceptance does not occur until the buyer has had a reasonable opportunity to inspect them; or
 - (c) does any act inconsistent with the seller's ownership; but if such act is wrongful as against the seller it is an acceptance only if ratified by him.
- (2) Acceptance of a part of any commercial unit is acceptance of that entire unit. (Footnote omitted.)

Buyer is liable for the purchase price of any goods accepted. MICH. COMP. LAWS ANN. § 400.2607(1) (1967). *See supra* note 88.

Additionally, buyer who has not yet accepted non-conforming goods has the right to reject them "if the goods or the tender of delivery fail in any respect to conform to the contract." MICH. COMP. LAWS ANN. § 440.2601 (1967). Buyer loses the right to reject when he accepts. MICH. COMP. LAWS ANN. § 440.2607(2) (1967). *See* J. WHITE & R. SUMMERS, HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE § 8-2 (2d ed. 1980).

94. 116 Mich. App. at 84, 322 N.W.2d at 551.

95. MICH. COMP. LAWS ANN. § 400.2606 (1)(a) (1967).

96. 116 Mich. App. at 86, 322 N.W.2d at 552.

What constitutes a reasonable opportunity to inspect depends on the facts and circumstances of the particular case. The prevailing view in cases involving consumers who purchase automobiles is that driving the car a short distance does not afford the buyer a reasonable opportunity to inspect. *See* J. WHITE & R. SUMMERS, HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE § 8-2 (2d ed. 1980). Where the defect in the car is mechanical, this approach is clearly correct. Perhaps a different view might be appropriate, however, where the defect is readily apparent or easily discoverable at the dealership.

Although he did not address the issue, the dissenter in *Colonial Dodge* must have concluded that buyer accepted the car, as his opinion focuses on revocation of acceptance. 116 Mich. App. at 87-89, 322 N.W.2d at 553-54 (Cynar, P.J., dissenting). *See* MICH. COMP. LAWS ANN. § 440.2608 (1967).

car were not inconsistent with seller's ownership.⁹⁷ Having thus concluded that buyer did not accept the car, the court originally held that buyer had an "absolute right" to reject it because it was non-conforming.⁹⁸

The result initially reached by the court of appeals is somewhat troubling: buyer has a right to reject an automobile that buyer has driven home and that is not in any way defective simply because seller failed to supply a spare tire due to a national tire strike. Unfortunately, the court on rehearing avoided consideration of this problem by finding that the parties agreed that buyer had accepted the car.⁹⁹

The relevant provision of the Code, which embodies the so-called perfect tender rule,¹⁰⁰ does appear literally to afford buyer the unqualified right to reject non-conforming goods, no matter how insubstantial or slight the nonconformity. The purpose served by literal application of that provision in cases involving minor nonconformities is, however, difficult to understand.¹⁰¹ Professors White and Summers suggest that courts avoid the troubling result—rejection granted for an insubstantial, if not slight, non-conformity—by manipulation of the procedural requirements for an effective rejection¹⁰² rather than

97. 116 Mich. App. at 86, 322 N.W.2d at 552. See MICH. COMP. LAWS ANN. § 440.2606(1)(c) (1967).

98. 116 Mich. App. at 86, 322 N.W.2d at 552.

99. 121 Mich. App. at 472, 328 N.W.2d at 679-80.

100. The Code section provides:

Subject to the provisions of this article on breach in installment contracts (section 2612) and unless otherwise agreed under the sections on contractual limitations of remedy (sections 2718 and 2719), if the goods or the tender of delivery fail in any respect to conform to the contract, the buyer may

- (a) reject the whole; or
- (b) accept the whole; or
- (c) accept any commercial unit or units and reject the rest.

MICH. COMP. LAWS ANN. § 440.2601 (1967). *But cf.* MICH. COMP. LAWS ANN. § 440.2608 (1967) (buyer may revoke acceptance only if the defect substantially impairs the value of the goods).

101. Under the Code parties to a contract have an obligation of good faith in the performance and enforcement of their agreement. MICH. COMP. LAWS ANN. § 440.1203 (1967). It has been suggested that where the nonconformity is slight and there is evidence that buyer is rejecting the goods as an excuse for getting out of a bargain, buyer might be precluded from exercising his right to reject because he is not doing so in good faith. See J. MURRAY, CONTRACTS § 176 (1974).

102. MICH. COMP. LAWS ANN. § 440.2602 (1967) provides;

- (1) Rejection of goods must be within a reasonable time after their delivery or tender. It is ineffective unless the buyer seasonably notifies the seller.
 - (2) Subject to the provisions of the 2 following sections on rejected goods (sections 2603 and 2604),
 - (a) after rejection any exercise of ownership by the buyer with respect to any commercial unit is wrongful as against the seller;
- and

outright refusal to apply the perfect tender rule.¹⁰³ That approach could not be taken in this case. Buyer gave seller prompt notice of rejection, and specified the reasons therefor.¹⁰⁴

A limitation on the perfect tender rule is seller's right to cure.¹⁰⁵ Its application in the instant case is, however, problematic. Seller presumably would have had a "further reasonable time to substitute a conforming tender."¹⁰⁶ It does not appear, however, that seller made any attempt to cure.¹⁰⁷

Having concluded on rehearing that buyer accepted the car, the court then properly found that buyer could not revoke acceptance because the non-conformity—a missing spare tire—did not substantially impair the value of the car.¹⁰⁸ Finally, given its finding that buyer accepted the car, the court reached the correct result—buyer is liable for the purchase price—albeit for the wrong reason.¹⁰⁹

(b) if the buyer has before rejection taken physical possession of goods in which he does not have a security interest under the provisions of this article (subsection (3) of section 2711), he is under a duty after rejection to hold them with reasonable care at the seller's disposition for a time sufficient to permit seller to remove them; but

(c) the buyer has no further obligations with regard to goods rightfully rejected.

(3) The seller's rights with respect to goods wrongfully rejected are governed by the provisions of this article on seller's remedies in general (section 2703).

Failure to make an "effective" rejection constitutes acceptance. MICH. COMP. LAWS ANN. § 440.2606(1)(b) (1967).

103. J. WHITE & R. SUMMERS, HANDBOOK ON THE LAW UNDER THE UNIFORM COMMERCIAL CODE § 8-3 (2d ed. 1980).

104. 116 Mich. App. at 87, 322 N.W.2d at 553. MICH. COMP. LAWS ANN. § 440.2602(1) (1967) requires buyer to seasonably notify seller of rejection. Buyer's failure to state the defect upon which rejection is based would preclude buyer from later relying on that defect to justify rejection or prove breach in cases where seller could have cured. MICH. COMP. LAWS ANN. § 440.2605 (1967).

105. The Code allows seller a limited right to cure where buyer has rejected non-conforming goods. MICH. COMP. LAWS ANN. § 440.2508 (1967). The policy is "to avoid injustice to the seller by reason of a surprise rejection by the buyer" in cases where seller had "reasonable grounds to believe" the tender would be acceptable. MICH. COMP. LAWS ANN. § 440.2508, Comment 2 (1967).

106. See MICH. COMP. LAWS ANN. § 440.2508(2) (1967).

107. 121 Mich. App. at 471; 328 N.W.2d at 679; 116 Mich. App. at 81, 322 N.W.2d at 550.

108. 121 Mich. App. at 473-74, 328 N.W.2d at 680. See MICH. COMP. LAWS ANN. § 440.2608 (1967). The dissent would find substantial impairment of value because of the danger of driving on Detroit area expressways in an improperly equipped automobile. 121 Mich. App. at 480, 328 N.W.2d at 683 (Deming, J., dissenting). See also *Colonial Dodge, Inc. v. Miller*, 116 Mich. App. 78, 82 n.1, 322 N.W.2d 549, 550 n.1 (1982).

109. Under the Code, a buyer who accepts goods is liable for the price. See

B. Rescission for Mutual Mistake

In *Lenawee County Board of Health v. Messerly*,¹¹⁰ the supreme court reexamined and correctly redirected the law respecting the consequences of mutual mistake. The mistake at issue in *Messerly* related to the belief of both buyer and seller of real property that the property conveyed could be used for income-generating purposes. The reality was to the contrary, as an inadequate septic system made the property unsuitable for human habitation.¹¹¹

In determining the significance of the mutual mistake, the court discussed two leading Michigan cases on the subject and wisely rejected their reasoning. The earlier cases, *Sherwood v. Walker*,¹¹² and *A & M Land Development Co. v. Miller*,¹¹³ when read in tandem, suggest that relief is available when the mistake affects the "essence" or "existence" of the subject matter of the contract,¹¹⁴ but may not be granted when it goes only to its "value" or "quality".¹¹⁵ Finding this

MICH. COMP. LAWS ANN. § 440.2709(1)(a) (1967). The court, having found that buyer accepted the car, should have simply so stated. Instead, the court turned to another provision of the Code (MICH. COMP. LAWS ANN. § 440.2709(1)(b) (1967)) and concluded that buyer is liable for the price because any effort by seller to resell the car would be unavailing. 121 Mich. App. at 476, 328 N.W.2d at 681.

110. 417 Mich. 17, 331 N.W.2d 203 (1982).

111. The Board of Health condemned the property, and obtained an injunction prohibiting human habitation of the premises. *Id.* at 21, 331 N.W.2d at 205. Buyer's claim for rescission was a counterclaim in response to seller's suit for foreclosure of the land contract, sale of property, and a deficiency judgment. *Id.*, 331 N.W.2d at 205-06. The trial court rejected buyer's claim for rescission and ordered foreclosure. The court held that the property was purchased "as is" and its "negative . . . value cannot be blamed upon an innocent seller." *Id.* at 22, 331 N.W.2d at 206. The court of appeals reversed and ordered rescission, concluding that the mutual mistake "went to a basic, as opposed to a collateral, element of the contract." *Id.* at 22-23, 331 N.W.2d at 206 (footnotes omitted).

112. 66 Mich. 568, 33 N.W. 919 (1887).

113. 354 Mich. 681, 94 N.W.2d 197 (1959).

114. In *Sherwood*, the parties' agreement was for the sale of a cow thought to be barren. Upon discovering that the cow was in fact fertile, seller refused to go through with the deal and sought rescission. In granting the requested relief, the court stated that the parties' mistake "went to the whole substance of the agreement." 66 Mich. at 577, 33 N.W. at 923. This mistake was not merely of the quality or value of the animal, "but went to the very nature of the thing. A barren cow is substantially a different creature than a breeding one." *Id.*

115. *A & M* involved a mistake which was deemed collateral to the agreement. In that case, the buyer of several lots of real estate sought partial rescission after failure to obtain permits from the health department to install septic tanks. Refusing rescission, the court stated:

There was here no mistake as to the form or substance of the contract between the parties, or the description of the property constituting the subject matter. . . . plaintiff received the property for which it contracted. The fact that it may be of less value than the purchaser expected at the time of the

distinction "inexact and confusing",¹¹⁶ the court abandoned it, and adopted a "better-reasoned approach":¹¹⁷ a case-by-case analysis using the test proposed by the *Restatement (Second) of Contracts*.¹¹⁸

Under the rule adopted in *Messerly*, rescission for mutual mistake is appropriate where (1) the mistake goes to a basic assumption on which the contract was made,¹¹⁹ and (2) the mistake has a material effect on the agreed exchange of performances,¹²⁰ unless (3) the party requesting rescission bears the risk of mistake.¹²¹ Applying this rule to the instant case, the court had no difficulty concluding that the mistake was fundamental and material because the erroneous assumption altered the character of the property conveyed and precluded the use of the property intended by the buyer.¹²² Nonetheless, the

transaction is not a sufficient basis for the granting of equitable relief. . . . 354 Mich. at 693-94, 94 N.W.2d at 203 (citation omitted).

116. 417 Mich. at 29, 331 N.W.2d at 209. The court aptly illustrated the difficulty of using the "essence" v. "value" test derived from *Sherwood* and *A & M* by attempting to apply it to the case before it. The instant mistake—the mistake in the assumption that the property was income-producing—"directly and dramatically" affected the value of the property, but also, without doubt, affected its essence; "[t]he thing' sold and bought [income-generating rental property] had in fact no 'existence'." *Id.* (citation omitted).

See also the court of appeals' 2-1 decision in *Messerly*, 98 Mich. App. 478, 295 N.W.2d 903 (1980). The split is based upon the diametrically opposed views of the majority and the dissenter on whether the mistake affected the "essence" or "value" of the contract.

117. 417 Mich. at 29, 331 N.W.2d at 209.

118. *Id.* at 29-30, 331 N.W.2d at 209-10. See *infra* notes 120 & 121.

119. *Id.* at 29, 331 N.W.2d at 209.

120. *Id.* RESTATEMENT (SECOND) OF CONTRACTS § 152 (1981) provides:

When a Mistake of Both Parties Makes A Contract Voidable

(1) Where a mistake of both parties at the time a contract was made as to a basic assumption on which the contract was made has a material effect on the agreed exchange of performances, the contract is voidable by the adversely affected party unless he bears the risk of the mistake under the rule stated in § 154.

(2) In determining whether the mistake has a material effect on the agreed exchange of performances, account is taken of any relief by way of reformation, restitution, or otherwise.

121. *Id.* at 30, 331 N.W.2d at 209-10. See *supra* note 120. RESTATEMENT (SECOND) OF CONTRACTS § 154 (1981) provides:

When a Party Bears the Risk of a Mistake

A party bears the risk of a mistake when

(a) the risk is allocated to him by agreement of the parties, or

(b) he is aware, at the time the contract is made, that he has only limited knowledge with respect to the facts to which the mistake relates but treats his limited knowledge as sufficient, or

(c) the risk is allocated to him by the court on the ground that it is reasonable in the circumstances to do so.

122. 417 Mich. at 30-31, 331 N.W.2d at 210.

supreme court reversed the court of appeals' grant of rescission.¹²³

Stating that the award of the equitable remedy of rescission rests in the discretion of the court,¹²⁴ the supreme court in *Messerly* concluded that rescission should be denied because the risk of mistake had been allocated by agreement of the parties to the buyer, who was the party seeking rescission.¹²⁵ The "as is" clause¹²⁶ in the purchase agreement was deemed to place the risk regarding unknown defects in the condition of the property upon the buyer.¹²⁷

On its facts, *Messerly* seems eminently correct. In *Messerly*, however, the supreme court did not have to face the far more difficult question of the proper allocation of risk when the agreement of the parties is silent on the point. That matter will no doubt be decided on a case-by-case basis.¹²⁸

C. Damages

1. Mental Distress

During the Survey period, the court of appeals decided several cases¹²⁹ involving claims of damages for mental distress stemming from a breach of contract. In each case the claim was denied.

123. *Id.* at 31, 331 N.W.2d at 210.

124. *Id.*

125. *Id.* at 32, 331 N.W.2d at 211.

126. The "as is" clause in *Messerly* provided: "Purchaser has examined this property and agrees to accept same in its present condition. There are no other or additional written or oral understandings." 417 Mich. at 21, 331 N.W.2d at 205.

127. *Id.* at 32, 331 N.W.2d at 211.

128. The court in *Messerly* gave no guidance regarding allocation of the risk of mistake absent agreement of the parties, except perhaps in its somewhat cryptic statement that had a risk of loss analysis been performed in *Sherwood v. Walker*, 66 Mich. 568, 33 N.W. 919 (1887), "the result might have been different." 417 Mich. at 31 n.13, 331 N.W.2d at 210 n.13.

Miller v. Varilek, 117 Mich. App. 165, 323 N.W.2d 637 (1982), a case decided by the court of appeals six months before *Messerly*, appeared to present this problem. The facts in *Miller* as reported by the court of appeals were substantially similar to those in *Messerly*. The parties entered into a land contract for the sale of lakefront property. After taking possession, buyer discovered that the septic system was inoperable. Buyer sued for rescission; seller counter-claimed for foreclosure. The only significant difference between *Miller* and *Messerly* appeared to be the absence of an "as is" clause in the *Miller* agreement. However, the decision of the court of appeals, remanding the case to the trial court with a mandate to follow the court of appeals' decision in *Messerly* in which rescission had been granted, was appealed to the Michigan Supreme Court. The supreme court in turn remanded to the court of appeals for reconsideration in light of the supreme court's decision in *Messerly*. *Miller v. Varilek*, 417 Mich. 998, 334 N.W.2d 376 (1983). On remand, the court of appeals reversed the original decision and affirmed the trial court's denial of rescission because the agreement of the parties in *Miller*, like the agreement of the parties in *Messerly*, contained an "as is" clause. *Miller v. Varilek*, No. 71552, (Mich. Ct. App. Oct. 24, 1983) (on remand).

129. *Valentine v. General Am. Credit, Inc.*, 123 Mich. App. 521, 332 N.W.2d

The lodestar for these decisions was *Kewin v. Massachusetts Mutual Life Insurance Co.*,¹³⁰ a 1980 decision of the Michigan Supreme Court. In *Kewin*, the court, after stating the general rule that damages recoverable for breach of contract are those that arise naturally from the breach or that are within the contemplation of the parties at the time the contract is made,¹³¹ announced a special rule for mental distress damages. In cases involving "commercial" contracts,¹³² damages are limited to the monetary value of the contract.¹³³ Damages for mental distress are cognizable only when "personal" contracts are at issue.¹³⁴

Guided by *Kewin*, the court of appeals denied claims for mental distress damages for breach of contract in cases involving (1) the pur-

591 (1983) (leave to appeal pending); *Chrum v. Charles Heating, Inc.*, 121 Mich. App. 17, 327 N.W.2d 568 (1982); *Groh v. Broadland Builders*, 120 Mich. App. 214, 327 N.W.2d 443 (1982).

130. 409 Mich. 401, 295 N.W.2d 50 (1980). In *Kewin*, the court held that a disability income protection policy was "commercial" in nature and mental distress damages, therefore, could not be recovered for mere breach. *Id.* at 419, 295 N.W.2d at 55.

131. *Id.* at 414, 295 N.W.2d at 52-53. The rule stated by the *Kewin* court is the rule of *Hadley v. Baxendale*, 156 Eng. Rep. 145 (1854).

132. Commercial contracts are those in which pecuniary interests predominate. 409 Mich. at 416, 295 N.W.2d at 53.

133. *Id.* at 414-15, 295 N.W.2d at 53. The assumption in breach of contract cases is that a party may be adequately compensated by reference to the terms of the contract alone. *Id.* at 417, 295 N.W.2d at 54.

By labeling insurance policies commercial in nature, the *Kewin* court was able to avoid the question of whether the particular insurance contract at issue implicated matters of mental concern and solicitude. *See Stewart v. Rudner*, 349 Mich. 459, 84 N.W.2d 816 (1957).

Before *Kewin*, several cases had allowed mental distress damages for breach of insurance contracts. *See Seaton v. State Farm Life Ins. Co.*, 75 Mich. App. 252, 254 N.W.2d 858 (1977); *Palmer v. Pacific Indem. Co.*, 74 Mich. App. 259, 254 N.W.2d 52, *leave to appeal denied*, 401 Mich. 808 (1977); *McCune v. Grimaldi Buick-Opel, Inc.*, 45 Mich. App. 472, 206 N.W.2d 742 (1973).

In an automobile insurance case decided during the Survey period, the court of appeals, following *Kewin* and its considerable progeny, denied plaintiff's claim for mental distress damages which was based solely on defendant's breach of a no-fault policy. *Butler v. Detroit Auto. Inter-Ins. Exch.*, 121 Mich. App. 727, 329 N.W.2d 781 (1982).

134. Personal contracts are those "concerned not with trade and commerce but with life and death, not with profit but with elements of personality, not with pecuniary aggrandizement but with matters of mental concern and solicitude" whereby a breach would "inevitably and necessarily result in mental anguish, pain and suffering". *Stewart v. Rudner*, 349 Mich. 459, 471, 84 N.W.2d 816, 824 (1957) (child stillborn due to doctor's failure to perform caesarean section as agreed upon).

Other Michigan cases illustrating *Stewart*-type contracts are *Allinger v. Kell*, 102 Mich. App. 798, 302 N.W.2d 576 (1981) (damages allowed for funeral director's mutilation of the body of plaintiff's murdered daughter); *Avery v. Arnold Home, Inc.*, 17 Mich. App. 240, 169 N.W.2d 135 (1969) (damages allowed for nursing homes' failure to alert plaintiff to his mother's impending death).

chase of a defective furnace which caused a fire that destroyed the buyer's home and its contents¹³⁵, (2) the construction of a home with a malfunctioning septic system,¹³⁶ and (3) employment.¹³⁷ These contracts were deemed "commercial", not "personal" and, accordingly, under *Kewin*, a per se bar existed to the grant of mental distress damages.¹³⁸

We question whether the distinction between "commercial" and "personal" contracts is as clear as *Kewin* suggests. The decision in the employment contract case¹³⁹ drew a strong dissent contending that an employment contract involved important personal rights and dignities, and was by no means solely commercial in nature.¹⁴⁰ Since mental and emotional distress are reasonably foreseeable results of breach of an employment contract, the dissent took the view that the trial court's award of a summary judgment on plaintiff's mental distress claim was inappropriate.¹⁴¹

There is much to be said for the position taken by the dissent. Contracts often have elements of both a commercial and a personal nature. Rather than attempting to squeeze a contract into one category or the other, a test based upon damages within the contemplation of the parties would seem to be the better approach.¹⁴²

2. Exemplary

The court of appeals dealt rather summarily with a claim for exemplary damages. In *Valentine v. General American Credit, Inc.*,¹⁴³ plaintiff requested punitive,¹⁴⁴ mental dis-

135. *Chrum v. Charles Heating, Inc.*, 121 Mich. App. 17, 327 N.W.2d 568 (1982).

136. *Groh v. Broadland Builders*, 120 Mich. App. 214, 327 N.W.2d 443 (1982).

137. *Valentine v. General Am. Credit, Inc.*, 123 Mich. App. 521, 332 N.W.2d 591 (1983) (leave to appeal pending).

138. In *Valentine*, the court, while concluding that the contract was commercial, noted that it would not necessarily view all employment contracts as such. Plaintiff in *Valentine* simply failed to state facts demonstrating that the contract had any personal aspects. *Id.* at 525-26, 332 N.W.2d at 593.

139. *Valentine v. General Am. Credit, Inc.*, 123 Mich. App. 521, 332 N.W.2d 591 (1983) (leave to appeal pending).

140. *Id.* at 530, 332 N.W.2d at 595 (Gillis, J., dissenting).

141. *Id.*

142. Justice Williams, in a lengthy dissent in *Kewin*, urged the court to adopt this approach. He argued that the disability insurance contract at issue in *Kewin* did involve matters of mental concern and solicitude, and that emotional distress damages were within the contemplation of the parties or arose naturally from the breach. 409 Mich. at 424, 295 N.W.2d at 57 (Williams, J., dissenting).

143. 123 Mich. App. 521, 332 N.W.2d 591, (leave to appeal pending) (1983).

144. The trial court granted defendant summary judgment. The court of appeals apparently affirmed the denial of plaintiff's claim for punitive damages,

truss,¹⁴⁵ and exemplary damages for breach of an employment contract. In affirming the trial court's entry of a summary judgment on the exemplary damages claim, the court of appeals simply quoted from *Kewin v. Massachusetts Mutual Life Insurance Co.*¹⁴⁶ for the proposition that "absent allegation and proof of tortious conduct existing independent of the breach . . . exemplary damages may not be awarded in common law actions brought for breach of a commercial contract."¹⁴⁷ The court concluded that plaintiff had made no such claim.¹⁴⁸

VI. MEDICAL MALPRACTICE ARBITRATION AGREEMENTS

Patients continue to argue that agreements entered into with doctors or hospitals to arbitrate malpractice disputes are unenforceable. The issues have not changed during this Survey period;¹⁴⁹ nor to any significant extent has the response of the court of appeals.

Challenges to the enforceability of these agreements are generally made on three grounds: (1) the Medical Malpractice Arbitration Act¹⁵⁰ (MMAA) is unconstitutional;¹⁵¹ (2) the agreements are uncon-

although the majority opinion fails to address the issue. The dissent did speak to it, but only to state that the claim was wholly without merit since "Michigan law prohibits an award of punitive damages." *Id.* at 531, 332 N.W.2d at 595 (citing *Kewin v. Massachusetts Mut. Life Ins. Co.*, 409 Mich. 401, 295 N.W.2d 50 (1980)).

145. See *supra* notes 129-42 and accompanying text.

146. 409 Mich. 401, 295 N.W.2d 50 (1980).

147. 123 Mich. App. at 525, 332 N.W.2d at 593 (quoting *Kewin v. Massachusetts Mut. Life Ins. Co.*, 409 Mich. 401, 295 N.W.2d 50 (1980)). For a discussion of the "commercial" contract versus "personal" contract distinction suggested in *Kewin*, see *supra* notes 130-42 and accompanying text.

148. 123 Mich. App. at 525, 332 N.W.2d at 593. Recovery of exemplary damages requires proof that defendant's conduct was malicious, wilful and wanton, and caused feelings of humiliation, outrage, and indignity. "The theory of these cases is that the reprehensibility of the defendant's conduct both intensifies the injury and justifies the award of exemplary damages as compensation for the harm done the plaintiff's feelings." 409 Mich. at 419, 295 N.W.2d at 55.

Mental distress and exemplary damages are considered duplicative; each is intended to compensate for injured feelings. Plaintiff may submit both theories to the jury, but recovery is limited to one. *Veselenak v. Smith*, 414 Mich. 567, 572, 327 N.W.2d 261, 263 (1982). See also *Valentine v. General Amer. Credit, Inc.*, 123 Mich. App. at 532, 332 N.W.2d at 596 (1983) (Gillis, J., dissenting) (leave to appeal pending).

149. See *W. Volz & D. Brouwer, Contracts*, 29 WAYNE L. REV. 491, 523-28 (1983).

150. MICH. COMP. LAWS ANN. §§ 600.5040 - .5065 (Supp. 1983-84).

151. See, e.g., *Lovell v. Sisters of Mercy Health Corp.*, 119 Mich. App. 44, 325 N.W.2d 619 (1982); *Horn v. Cooke*, 118 Mich. App. 740, 325 N.W.2d 558 (1982); *Christman v. Sisters of Mercy*, 118 Mich. App. 719, 325 N.W.2d 801 (1982); *Gale v. Providence Hosp.*, 118 Mich. App. 405, 325 N.W.2d 439 (1982); *Strong v. Oakwood Hosp. Corp.*, 118 Mich. App. 395, 325 N.W.2d 435 (1982); *Murray v. Wilner*, 118

cionable;¹⁵² and (3) the agreements are contracts of adhesion.¹⁵³ Additionally, patients contend that arbitration agreements cannot be enforced against them absent a showing by the doctor or hospital of a knowing, intelligent, and voluntary waiver by the patient of the constitutional right of access to the courts.¹⁵⁴

A. *Constitutionality of the MMAA*

The court of appeals is sharply divided over the constitutionality of the MMAA.¹⁵⁵ Several cases were decided during the Survey period.¹⁵⁶ In all but one¹⁵⁷ the court struck down the MMAA on constitutional grounds.

Mich. App. 352, 325 N.W.2d 422 (1982); *Jackson v. Detroit Mem. Hosp.*, 110 Mich. App. 202, 312 N.W.2d 212, *leave to appeal granted*, 412 Mich. 885 (1981); *Morris v. Metriyakool*, 107 Mich. App. 110, 309 N.W.2d 910, *leave to appeal granted*, 412 Mich. 884 (1981); *Brown v. Siang*, 107 Mich. App. 91, 309 N.W.2d 575 (1981).

152. *See, e.g.*, *Gale v. Providence Hosp.*, 118 Mich. App. 405, 325 N.W.2d 439 (1982); *Strong v. Oakwood Hosp. Corp.*, 118 Mich. App. 395, 325 N.W.2d 435 (1982); *Murray v. Wilner*, 118 Mich. App. 352, 325 N.W.2d 422 (1982); *Jackson v. Detroit Mem. Hosp.*, 110 Mich. App. 202, 312 N.W.2d 212, *leave to appeal granted*, 412 Mich. 885 (1981); *Morris v. Metriyakool*, 107 Mich. App. 110, 309 N.W.2d 910, *leave to appeal granted*, 412 Mich. 884 (1981).

153. *See, e.g.*, *Gale v. Providence Hosp.*, 118 Mich. App. 405, 325 N.W.2d 439 (1982); *Strong v. Oakwood Hosp. Corp.*, 118 Mich. App. 395, 325 N.W.2d 435 (1982); *Murray v. Wilner*, 118 Mich. App. 352, 325 N.W.2d 422 (1982); *Jackson v. Detroit Mem. Hosp.*, 110 Mich. App. 202, 312 N.W.2d 212, *leave to appeal granted*, 412 Mich. 885 (1981); *Morris v. Metriyakool*, 107 Mich. App. 110, 309 N.W.2d 910, *leave to appeal granted*, 412 Mich. 884 (1981).

154. *See, e.g.*, *Moore v. Fragatos*, 116 Mich. App. 179, 321 N.W.2d 781 (1982); Brief for Appellee at 7-8, *Jackson v. Detroit Mem. Hosp.*, 110 Mich. App. 202, 312 N.W.2d 212, *leave to appeal granted*, 412 Mich. 885 (1981); Brief for Appellant at 7, *Morris v. Metriyakool*, 107 Mich. App. 110, 309 N.W.2d 910, *leave to appeal granted*, 412 Mich. 884 (1981).

155. *Compare* *Strong v. Oakwood Hosp. Corp.*, 118 Mich. App. 395, 325 N.W.2d 435 (1982); *Murray v. Wilner*, 118 Mich. App. 352, 325 N.W.2d 422 (1982); *Jackson v. Detroit Mem. Hosp.*, 110 Mich. App. 202, 312 N.W.2d 212, *leave to appeal granted*, 412 Mich. 885 (1981); *Piskorski v. Art Centre Hosp.*, 110 Mich. App. 22, 312 N.W.2d 160 (1981) *with* *Horn v. Cooke*, 118 Mich. App. 740, 325 N.W.2d 558 (1982); *Cushman v. Frankel*, 111 Mich. App. 604, 314 N.W.2d 705 (1981); *Williams v. O'Connor*, 108 Mich. App. 613, 310 N.W.2d 825 (1981); *Morris v. Metriyakool*, 107 Mich. App. 110, 309 N.W.2d 910, *leave to appeal granted*, 412 Mich. 884 (1981).

156. *Lovell v. Sisters of Mercy Health Corp.*, 119 Mich. App. 44, 325 N.W.2d 619 (1982); *Horn v. Cooke*, 118 Mich. App. 740, 325 N.W.2d 558 (1982); *Christman v. Sisters of Mercy*, 118 Mich. App. 719, 325 N.W.2d 801 (1982); *Gale v. Providence Hosp.*, 118 Mich. App. 405, 325 N.W.2d 439 (1982); *Strong v. Oakwood Hosp. Corp.*, 118 Mich. App. 395, 325 N.W.2d 435 (1982); *Murray v. Wilner*, 118 Mich. App. 352, 325 N.W.2d 422 (1982); *Strong v. Pontiac Gen. Hosp.* 117 Mich. App. 143, 323 N.W.2d 629 (1982).

157. *Horn v. Cooke*, 118 Mich. App. 740, 325 N.W.2d 558 (1982). The court remanded for an evidentiary hearing on the patient's claim that the arbitration agree-

Plaintiffs challenging the MMAA consistently contend that it violates the due process clauses of the Constitutions of the United States¹⁵⁸ and the State of Michigan.¹⁵⁹ Specifically, it is alleged that because the MMAA requires a health care provider to be one of the three members of the arbitration panel,¹⁶⁰ patients are deprived of a fair hearing before an impartial decision-maker.¹⁶¹

Two sources of bias or partiality are advanced: health care providers have a pecuniary interest in the outcome of these arbitrations,¹⁶² and in the context of a malpractice controversy, will

ment was obtained by fraudulent misrepresentation. *Id.* at 749, 325 N.W.2d at 562.

Two judges of the court of appeals, N.J. Kaufman and D. Riley, changed their positions regarding the constitutionality of the MMAA. Both had previously found the MMAA constitutional and each wrote an opinion explaining the reasons for now holding the contrary view. *See Murray v. Wilner*, 118 Mich. App. 352, 325 N.W.2d 422 (1982); *Strong v. Oakwood Hosp. Corp.*, 118 Mich. App. 395, 325 N.W.2d 435 (1982).

The seven cases decided during the Survey period do not appear to be representative of the views of the members of the court of appeals to the extent they suggest substantial agreement that the MMAA is unconstitutional. In fact, in *Horn v. Cooke*, 118 Mich. App. 740, 325 N.W.2d 558 (1982), the court of appeals stated: "The majority of the members of the Court who have ruled on this issue have found that the Act is constitutional." *Id.* at 749, 325 N.W.2d at 562.

158. U.S. CONST. amend. XIV, § 1.

159. MICH. CONST. art. 1, § 17.

160. The MMAA provides:

An arbitration under this chapter shall be heard by a panel of 3 arbitrators. One shall be an attorney who shall be the chairperson and shall have jurisdiction over prehearing procedures, 1 shall be a physician, preferably but not necessarily from the respondent's medical specialty, and the third shall be a person who is neither a licensee of the health profession involved, a lawyer, nor a representative of a hospital or an insurance company. Where a case involves a hospital only, a hospital administrator may be substituted for a physician. If a case involves a health care provider other than a physician, a licensee of the health profession involved may be substituted for a physician.

MICH. COMP. LAWS ANN. § 600.5044(2) (Supp. 1982-83).

161. *See, e.g., Murray v. Wilner*, 118 Mich. App. 352, 325 N.W.2d 422 (1982); *Strong v. Oakwood Hosp. Corp.*, 118 Mich. App. 395, 325 N.W.2d 435 (1982); *Jackson v. Detroit Mem. Hosp.*, 110 Mich. App. 202, 312 N.W.2d 212, *leave to appeal granted*, 412 Mich. 885 (1981); *Morris v. Metriyakool*, 107 Mich. App. 110, 309 N.W.2d 910, *leave to appeal granted*, 412 Mich. 884 (1981).

162. The United States Supreme Court has held that a person's due process right to a hearing before a fair and impartial tribunal is violated where the decision-maker has a direct pecuniary interest in the outcome of the case. *See Gibson v. Berryhill*, 411 U.S. 564 (1973); *Ward v. Monroeville*, 409 U.S. 57 (1972); *Tumey v. Ohio*, 273 U.S. 410 (1927). *See also Crampton v. Department of State*, 395 Mich. 347, 235 N.W.2d 352 (1975). Patients contend that because the number and size of malpractice awards affect directly the availability and cost of medical malpractice insurance, health care providers have a direct economic interest in minimizing those awards. *See, e.g., Murray v. Wilner*, 118 Mich. App. at 363-65, 325 N.W.2d at 428-29.

align themselves with the doctor, a member of their own profession, against the patient.¹⁶³

B. *Unconscionability*

Until this Survey period, no panel of the court of appeals had found meritorious the claim that medical malpractice arbitration agreements were unconscionable.¹⁶⁴ Now, however, Judges Cynar and Riley, who sat together on the panels that decided three of the seven cases reported last year,¹⁶⁵ agree that these contracts are unconscionable. The "inherent disproportionate bargaining position" between a patient and a hospital or doctor,¹⁶⁶ and the substantive unreasonableness of these agreements,¹⁶⁷ persuaded Judge Riley that they are unconscionable. Judge Cynar's determination of unconscionability rested on the somewhat different basis that the patient lacked a meaningful opportunity to decide whether to forego the constitutional right of access to the courts.¹⁶⁸

In responding to these views, Judge Maher indicated agreement that enforcement of these contracts is unwise, but stated that the legislature, in adopting the MMAA, has declared the state's public policy, a declaration that cannot be judicially overridden by holding these contracts unconscionable.¹⁶⁹

C. *Contracts of Adhesion*

No panel of the court of appeals has found these agreements to be "take-it-or-leave-it" contracts of adhesion.¹⁷⁰ A patient can obtain medical treatment without entering into an arbitration agreement.¹⁷¹

163. "The pertinent issue is not whether a particular group or profession is or is not fair-minded, but whether the function and frame of reference of such persons may be expected to make them partisan to their fellows." *Murray v. Wilner*, 118 Mich. App. at 361, 325 N.W.2d at 427. See *Crampton v. Department of State*, 395 Mich. 347, 235 N.W.2d 352 (1975).

164. "The panels have been unanimous in rejecting claims that the arbitration agreement form is unconscionable or an adhesion contract (citations omitted). We agree that these claims are without merit." *Murray v. Wilner*, 118 Mich. App. at 355-56, 325 N.W.2d at 424-25.

165. *Lovell v. Sisters of Mercy Health Corp.*, 119 Mich. App. 44, 325 N.W.2d 619 (1982); *Gale v. Providence Hosp.*, 118 Mich. App. 405, 325 N.W.2d 439 (1982); *Strong v. Oakwood Hosp. Corp.*, 118 Mich. App. 395, 325 N.W.2d 435 (1982).

166. 118 Mich. App. at 401-02, 325 N.W.2d at 438.

167. *Id.* at 402-03, 325 N.W.2d at 438.

168. 118 Mich. App. at 411, 325 N.W.2d at 441.

169. 118 Mich. App. at 403-04, 325 N.W.2d at 439.

170. See *Strong v. Oakwood Hosp. Corp.*, 118 Mich. App. at 400, 325 N.W.2d at 437; *Murray v. Wilner*, 118 Mich. App. at 355-56, 325 N.W.2d at 424.

171. A health care provider who conditions treatment on the signing of an arbitration agreement violates the MMAA. MICH. COMP. LAWS ANN. § 600.5041(2)

Additionally, patients have sixty days after agreeing to arbitration to withdraw from the contract.¹⁷²

We are of the view that further comment upon these issues is not now warranted. These matters have been briefed and argued before the supreme court¹⁷³ and a decision should soon be reached, quite possibly before this Survey is in print. After the supreme court speaks, a full analysis will be possible, an analysis best left to the next Survey.

(Supp. 1982-83). See *Capman v. Harper Grace Hosp.*, 96 Mich. App. 510, 294 N.W.2d 205 (1980). See also *Horn v. Cooke*, 118 Mich. App. 740, 325 N.W.2d 558 (1982).

172. MICH. COMP. LAWS ANN. § 600.5041(1), (3) (Supp. 1982-83).

173. *Morris v. Metriyakool*, 107 Mich. App. 110, 309 N.W.2d 910, *leave to appeal granted*, 412 Mich. 884 (1981); *Jackson v. Detroit Mem. Hosp.*, 110 Mich. App. 202, 312 N.W.2d 212, *leave to appeal granted*, 412 Mich. 885 (1981). Eight other cases have been held in abeyance pending the outcome of *Morris* and *Jackson*: *Lovell v. Sisters of Mercy Health Corp.*, 119 Mich. App. 44, 325 N.W.2d 619 (1982); *Murray v. Wilner*, 118 Mich. App. 352, 325 N.W.2d 422 (1982); *Strong v. Oakwood Hosp. Corp.*, 118 Mich. App. 395, 325 N.W.2d 435 (1982); *Malek v. Jayakar*, 116 Mich. App. 111, 321 N.W.2d 858 (1982); *Rome v. Sinai Hosp.*, 112 Mich. App. 387, 316 N.W.2d 428 (1982); *Cushman v. Frankel*, 111 Mich. App. 605, 314 N.W.2d 705 (1981); *Piskorski v. Art Centre Hosp.*, 110 Mich. App. 22, 312 N.W.2d 441 (1981); *Brown v. Siang*, 107 Mich. App. 91, 309 N.W.2d 575 (1981).