



## The Spirit of the Law

From very early times, the law has not enforced **gratuitous**, or free agreements. Agreements must be bargained for if they are to be binding on those who are parties to them. An agreement is bargained for when (1) a promise is made in exchange for another promise, (2) a promise is made in exchange for an act, or (3) a promise is made in exchange for a forbearance to act. The idea is that, if in relying on another's promise someone gives up nothing, he or she is not injured if the promise is not kept. What is given up is consideration.

### Legal Issues:

1. When someone is under a contractual duty to do something, is a promise to give additional property to do the same thing binding?
2. Is a promise to give money in exchange for something that has already been done binding?
3. Are social promises enforceable in a court of law?
4. If the parties to a contract disagree on the amount owed, will the payment of a lesser amount discharge the debt?
5. Is a pledge to a charity binding?

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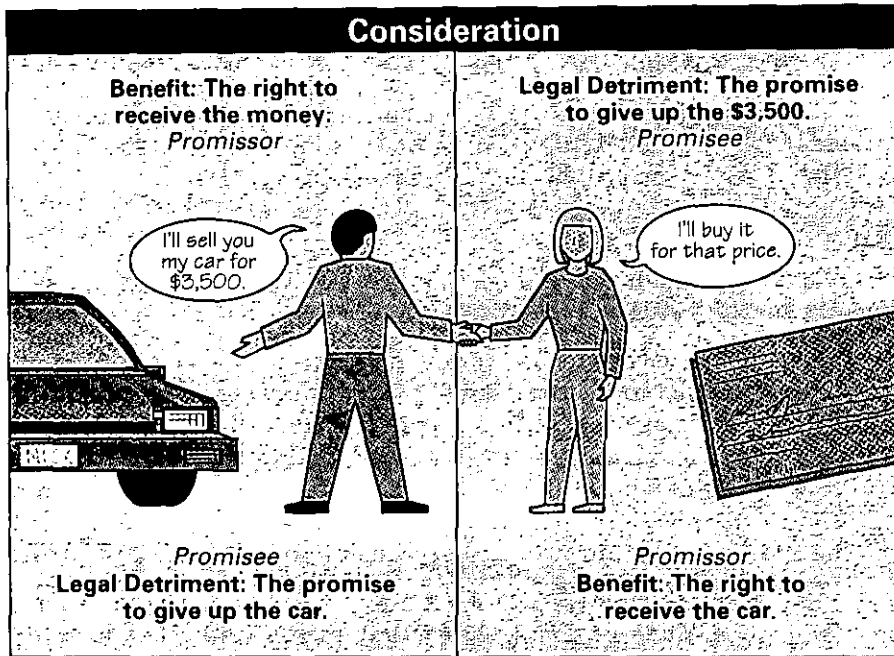
## Consideration

You know that a contract must contain six essential elements. We have already looked at offer, acceptance, genuine agreement and capacity. The next element to review is consideration. **Consideration** is the exchange of benefits and detriments by the parties to an agreement. A **benefit** is something that a party was not previously entitled to receive. A **detriment** is any loss suffered. There are three types of detriment. The first involves giving up something, or promising to give up something, that you have a legal right to keep. Promising to sell something is an example of giving up something that you have a legal right to. A second type of detriment involves doing something, or promising to do something, that you have a legal right not to do. Promising to paint someone's house is an example of doing something that you have a legal right not to do.

A third type of detriment involves **forbearance**, or not doing something that you have the legal right to do. Eddie's promise not to void his contract with Jake is an example of forbearance. Eddie has the legal right to void his contract with Jake for the CD player. He has agreed not to void that contract. In exchange, Eddie has demanded that Jake give him one-half of the CD's in his collection. This is a new contract supported by Eddie's forbearance. Another common forbearance is a promise not to bring a lawsuit.

*Example 1.* Suppose that you agree to sell your CD player to Carol Adams for \$50. Adams agrees to buy it at that price. You have made a promise to sell. Adams has made a promise to buy. Each promise is consideration for the other.

Your benefit is your right to receive the \$50. Your detriment is your promise to give up the CD player. Adams' benefit is the right to receive the CD player. Her detriment is her promise to give up the \$50. This is the most common way that consideration occurs in contracts. It is found in the promises of the parties. Figure 10-1 illustrates how this exchange takes place.



**Figure 10-1** Consideration is an exchange of benefits and detriments by the parties to an agreement. Is consideration required to make an agreement legally binding?

## Agreements Without Consideration

Certain acts and promises do not provide consideration. These include promises to make a gift, to obey the law, or to fulfill another preexisting duty. In addition, past consideration and illusory promises are not consideration at all.

### *Promise to Make a Gift*

A gift is something given freely, for no consideration. Once given, a gift has the status of an executed contract, and the giver cannot force its return. However, the promise to make a gift is not enforceable and does not constitute a contract.

**Example 2.** Pete's favorite uncle, Steve, promises Pete a gift of \$1,000 cash with no strings attached. His uncle tells him, "You are honorable. Your grades are excellent. You are also a great help to your parents at home. Next Tuesday I am going to give you \$1,000 as a gift because I like you. Is that acceptable to you?" Pete replies, "Yes!"

In this example, there is no consideration for Steve's promise because Pete gave nothing up (and promised nothing) and, therefore, suffered no detriment. Similarly, Steve received no benefit from the transaction. If Steve refuses to make the gift, Pete cannot sue him for breach of contract. If the gift were made, however, it would be Pete's property.

**LAW & Ethics**

Juan promises to pay Maria \$1,000 if she will marry him. She agrees. After they are married, Juan refuses to pay. What are the ethical issues? Is this a break of contract?

## Promise to Obey the Law

Since everyone is obligated to obey the law, a promise to do so is no detriment.

**Example 3.** Suzanne Culman was arrested for smoking marijuana, a criminal offense in her state. Her Aunt Sylvia wrote to her, "If you will stop smoking, I will give you \$2,000." Culman stopped smoking, but her aunt refused to give her the money.

Culman cannot enforce the agreement because it contained no valid consideration. Culman refrained from doing something that she had no legal right to do anyway; thus, she suffered no legal detriment.

## Preexisting Duty

If a person is already under a legal duty to do something, a promise to do that same thing does not furnish consideration.

**Example 4.** A city council offered a reward to anyone who gave information that led to the conviction of the person who had been setting fires. In addition, the city hired a night watchman to be on the lookout for anyone setting fires. The night watchman caught the person setting fires and sought the reward. The court held that he was not entitled to the reward because he was under a legal duty to do what he did and thus did not furnish consideration to the city for its promise to pay the reward.

Similarly, if someone already has a duty under a contract to do something, a promise to do that same thing does not furnish consideration.

**Example 5.** Morgan contracted to work for Davis for one year for \$200 per week. After starting the job, another company offered Morgan \$250 per week to do the same work. Morgan told Davis about the new offer, and Davis said to him, "Stay on with me and I'll give you a \$1,200 bonus at the end of the year." Morgan finished the year, but Davis refused to give him the bonus as he had agreed. The court held that Morgan was not entitled to the bonus; he gave no consideration for it, since he was under a contractual duty to work for Davis for the entire year.

In answer to Legal Issue 1, Davis was not bound to pay Morgan the bonus. However, parties to a contract can always end it by mutual consent. Thus, in the example above, Morgan and Davis could have ended the old contract and formed a new one containing the new terms. In that case, Morgan could have enforced the promise for the \$1,200 bonus.

## Past Consideration

Giving or exchanging benefits and detriments by the parties must take place when the contract is made. If consideration took place in the past or is given for something that has already been done, the courts will not regard the consideration as legal. The courts will not enforce any contract based on past consideration.

**Example 6.** In the opening vignette, Jake promises to pay Tony \$5 for his "valuable legal advice." However, Tony had already advised

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Jake with no expectation of payment. Therefore, in answer to Legal Issue 2, Jake would have no legal obligation to pay Tony that \$5. Jake's promise was the result of Tony's past performance. No consideration passed from Tony to Jake for the money. In addition, note that Jake has actually offered to give Tony a gift. A promise of a gift cannot be enforced by a court.

### *Illusory Promise*

For a binding contract to be formed, both parties must be under obligation to do something; otherwise, neither is bound to do anything. Some contracts are **illusory**; they have a false appearance. At first glance, they appear to bind both parties. Upon further examination, however, it is clear that they do not.

*Example 7.* Isadore Karras agreed to sell, and Lorraine Patti agreed to buy, at a stated price per bushel, all the potatoes that Patti might order within the next two months. Because Patti might not order any potatoes within the next two months, she is not bound to do anything. The contract is illusory.

### *Promise to Attend a Social Engagement*

All contracts consist of agreements, but not all agreements consist of contracts. An agreement to meet a friend for lunch would not be a legally enforceable agreement, because the friend has given nothing in exchange for that promise. Thus, that agreement lacks consideration. In answer to Legal Issue 3, the courts have never been inclined to enforce social agreements such as dates, dinner engagements, and the like. In the opening vignette, Tony's Uncle Angelo made an agreement to meet his army buddy, Roscoe, on State Street at a prearranged date and time. Roscoe never showed up. Angered by this, Angelo has threatened to sue his friend Roscoe. However, since this qualifies as a social agreement, Angelo will find that he has no grounds for a lawsuit.

## **Adequacy of Consideration**

Generally, the courts do not look into the adequacy of the consideration. That is, they do not look to see whether the value of the consideration was fair to both parties. They let the parties make their own valid agreement and usually enforce that agreement.

*Example 8.* Lynne Turner sees a statuette marked \$500 in an antique shop. She offers the proprietor \$400 for the statuette, and the proprietor accepts. Later, Turner discovers that the figure is a cheap import worth not more than \$10. She argues that there was no consideration for her promise to pay.

Turner will have to pay \$400 as she agreed. The court will not consider the inadequacy of the consideration. However, if the store proprietor had falsely represented that the statuette was a genuine antique and very valuable, the inadequacy of the consideration could be used along with other evidence to show fraud. The contract could then be set aside on the grounds of fraud.

### **FYI**

In common law, a seal took the place of consideration. Parties to a contract would melt wax onto the paper and press into it a ring or personal seal. Contracts under seal were used when most people could not read or write. They dictated contracts to writers and placed their seal on the document to show their agreement.

Occasionally, however, a court may refuse to enforce a contract or a portion of it. This exception occurs when the consideration is so inadequate that it shocks the conscience of the court. The court finds the contract unconscionable, that is, the contract is so one-sided that it unfairly oppresses one party and unreasonably favors the other party. This usually occurs in situations in which there is a vast difference between the parties in bargaining power. If a court, as a matter of law, finds a contract or any clause of a contract to have been unconscionable at the time it was made, the court may do one of three things. It may refuse to enforce the contract. It may enforce the contract minus the unconscionable clause. Or, it may limit the application of any unconscionable clause so as to avoid any unconscionable result.

*Example 9.* Mrs. O'Grady, an 85-year-old widow, lived alone in a small bungalow. A fast-talking, door-to-door salesperson talked her into signing a contract to have vinyl siding put on her house for \$40,000. A fair price for the job would have been about \$4,000. Because of the difference in bargaining power of the parties and the exceptionally unfair price, it is unlikely that a court would enforce this contract.

If a contract is claimed to be or appears unconscionable, the court may give the parties a reasonable opportunity to present evidence concerning the commercial setting of the contract. This could include the purpose and effect of the contract to aid the court in making a decision. In examining the commercial setting, the court will look at the needs and practices of a particular trade or business to determine what is or is not accepted practice. What may seem unfair and unconscionable in one trade may be considered fair and reasonable in another.

## Special Applications of Consideration

Each promise made as consideration for another promise must create a new obligation. If you promise to do something you are already legally bound to do, your promise does not create a new obligation and is not regarded as valid consideration.

### *Partial Payment of a Debt*

*Example 10.* Roger Bolton owes Guy Racine \$300. Bolton admits that the money is owed and that payment is overdue. Racine is pressuring Bolton for payment and states, "If you will pay me \$200, I will cancel the \$300 debt." Bolton agrees and pays the \$200, relying on Racine's promise. The following day Racine sues Bolton for the remaining \$100.

Bolton will have to pay the \$100. Racine's promise to forgive the balance is not binding on him because there was no consideration for it. Bolton paid the \$200, relying on Racine's promise. But Bolton already owed the \$300; he was promising to do something that he was already legally bound to do. If Racine's release had been in writing and signed by Racine, it would have been binding in some states. Other states would require a seal in addition to the writing to make it binding.

*Example 11.* Suppose, in Example 10, that the \$300 Bolton owed Racine is not due for another month. Suppose also that Racine says to Bolton, "If you will pay me \$200 today, I will cancel the \$300 debt."

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Bolton agrees and pays the \$200. Racine cannot sue for the balance because Bolton has paid the debt before it was due. This provides consideration for Racine's promise to cancel the debt.

### Settlement of Disputed Claims

Suppose that there is an honest difference of opinion as to how much is owed. Parties often compromise on the amount owed, particularly in contracts for services.

**Example 12.** Clarence Judd claims that Terry Dees owes him \$100 for typing services, but Dees maintains that she owes only \$50. Judd thinks that the typing services were worth \$100. Dees thinks that they were worth only \$50. If Dees compromises on \$75, each has given up something, and the agreement is binding.

When you visit a doctor or take your car to a garage for repairs, unless a price is agreed on before the work is done, you are implying that you promise to pay the reasonable value of the services. The bill you receive for the services may be more than this. People sometimes handle this situation by sending a check for what they consider to be a reasonable amount. They write on the check the words "In full payment of the amount I owe you." If the amount really is in dispute or not agreed upon, the cashing of the check is treated as the acceptance of the smaller amount, and the balance cannot be recovered.

## Law in Other Cultures

### Native American Groups

In 1988 the members of the Puyallup group voted to accept an offer from the city of Tacoma, Washington. The Puyallup group agreed to exchange its rights to nearly \$1 billion of real estate in downtown Tacoma for more useful land as well as money to help the group and its members. The consideration the Puyallup group received included 900 acres of land, a trust fund, and a cash grant for each adult member of the group. In addition, the Puyallup group received \$61 million to set up a salmon fishery and a marne terminal to employ its members. The deal was negotiated by Senator Daniel Inouye, chairman of the Select Committee on Indian Affairs.

The relationship between Native American groups and the United States government is unique. Although Native American reservations are part of the United States, many of the laws that govern the Native American citizens who live on those reservations differ from those that govern other U.S. citizens.

The U.S. government enforces special laws to protect certain Native American lands and the Native Americans whose lives those lands affect. Under these laws, contract documents for agreements that relate to certain Native American lands must meet special requirements, in addition to the usual six requirements for a contract. For instance, the contracts must be approved by two officials—the Secretary of the Interior and the Commissioner of Indian Affairs. Both officials must show their approval by signing the formal contract document. Thus, although Native Americans or Native American groups own the land, their rights to sale or use of the land are restricted.

1. What does the U.S. government do to protect certain Native American lands?
2. What two officials must approve agreements that relate to certain Native American lands?

Note, however, that the amount must really be in dispute. In the opening vignette, Tony argues that he should not have to pay three dollars for the sodas because last week the same sodas would have cost half that amount. Thus, it appears as if the amount is in dispute. However, since the price of the sodas was clearly printed on the menu, the amount that Tony would owe after the purchase of the sodas was never really in dispute. He was just caught by surprise because he did not bother to read the menu. As we have already seen, failure to read a document that makes up a contract will not excuse a party from performing according to the terms of the writing. Therefore, in answer to Legal Issue 4, even though the waitress accepted half the amount due, Tony still owes Kowalski's Deli \$1.50.



▲Customers and business owners sometimes disagree over the exact terms of a service after that service has been performed. In what ways can such disputes be resolved?

### *Extension of Time for Payment*

Now let's look at the situation above from the Deli's viewpoint. The bill that Tony ran up at the Deli was due and payable at the time that he and the others received the sodas. Tina, the waitress, agreed to accept half of the amount due and to extend the time of payment for the other half in exchange for Tony's agreement to pay the next time he is in the Deli. Tony agreed. However, if Mr. Kowalski stopped Tony before he left the Deli and demanded immediate payment, Tony would be required to pay the amount remaining or suffer the consequences. The amount in question is so small that it is likely Tony would either pay up or wash a few dozen dishes for Mr. Kowalski to work off the debt.

Let's look at an example that involves a slightly larger amount of money and slightly more serious legal consequences.

*Example 13.* TerraForm International owes an agreed amount of \$1 million to The World Bank and Trust Co. The debt is now due and payable, but TerraForm International does not have the money. Clarence Jefferson, the vice president of the bank, promises to extend the time of

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payment 30 days if TerraForm will agree to pay at that time. Jeff Ridgeway, the president of TerraForm International, gives his promise. The next day, however, Jefferson rescinds the promise and brings suit against TerraForm International.

The bank is not bound by his promise to extend the time of payment. TerraForm, through Ridgeway, promised nothing new, and thus there is no consideration for the promised extension. Some states have changed this rule by statute.

## Promises Enforceable Without Consideration

Some promises are enforceable without consideration. In certain circumstances the courts find that a promise influences the behavior of other people. If such promises were not enforced, those relying on them may suffer damages. These special cases include pledges and subscriptions to charities and promissory estoppel.

### *Pledges and Subscriptions*

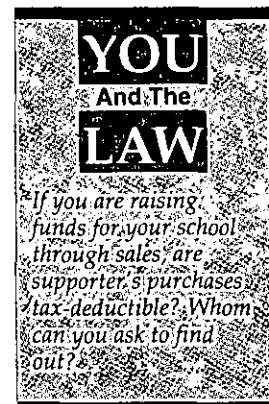
Citizens and business firms are often asked to sign pledges to support community projects. This is what happened in the opening vignette, when Mr. Santini asked Tony, Juleanne, and Jake to sign pledge cards for the National Charities campaign. Technically speaking, Tony was correct when he pointed out that a pledge is a promise to make a gift and is not based on formal consideration. However, in answer to Legal Issue 5, because such pledges usually involve charitable projects and are, therefore, in the public interest, the courts usually try to find some way to enforce them.

Not all courts look at consideration for pledges or subscriptions in the same way. Some courts hold that the promises of other persons who have subscribed to the same fund amount to consideration. Other courts hold that if the charitable institution had made commitments to spend the money as a result of relying on such subscriptions, the subscriptions are enforceable. Still other courts hold that there is an implied promise on the part of the institution to use the funds in the manner designated and that this promise amounts to consideration.

**Example 14.** Arcadia Community and Technical College (ACTC) held a fund drive to raise \$5 million for the construction of a new engineering center. Disanto Industries, Inc., pledged to donate \$1 million to the ACTC building fund. The construction was completed one year later. Under the laws of that state, the construction work that was completed by ACTC in reliance on Disanto's pledge formed the consideration, making the pledge binding and enforceable.

### *Promissory Estoppel*

Under the doctrine of **promissory estoppel**, a promise may be enforceable without consideration. The word *promissory* means "containing or consisting of a promise." The word *estoppel* means "restraint on a person to prevent him or her from contradicting a previous act." The





doctrine is used on occasion to prevent injustice when one changes one's position significantly in reliance on another's promise, and the promise is not fulfilled. The court will "estop" the person who made the promise from claiming that there was no consideration. Certain conditions must be met, however, before a court will apply this principle. First, the promise must be made to bring about action or forbearance by another person who gave no consideration. Second, the one who gave no consideration must have relied on the promise and changed his or her position in a significant way. Third, injustice can be avoided only by enforcing the promise.

*Example 15.* Hosuk Chai, knowing that his niece, Jill Chai, wishes to go to college and has no money to do so, promises to give her \$40,000 when she graduates. Jill quits her job, borrows money, goes into a great deal of debt, and graduates from college. Hosuk then notifies his niece that he has changed his mind about the \$40,000 gift. To prevent injustice, the court may "estop" Hosuk from claiming that Jill gave no consideration for his promise.

## Reducing Legal Risks

Analyze all contracts to ensure that valid consideration is present. If you are in doubt, get legal advice. Remember that the courts will not enforce the promise of a gift unless there is also a promise on your part. Before entering an agreement, obtain a written statement from the promisor.

## Consideration in Your Everyday Life

The following principles pertain to consideration in everyday situations:

- To amount to consideration, the act done or promised must be legal and not involve any violation of the law.
- If a person pays a debt in advance, it is something he or she is not legally bound to do. This would amount to consideration for settling the debt for a lesser amount.
- If a person has made a gift in the past, has performed services in the past as a gift, or has been paid for past services, he or she may not use these past performances as consideration for a new promise.
- To constitute consideration, an act or a promise must be bargained for.

## Chapter

# 10 Review



### Summary

Carefully read the summary below before completing the chapter review.

1. Consideration is the exchange of benefits and detriments by the parties to an agreement. A benefit is something that a party was not previously entitled to receive. A detriment is any loss suffered. The three types of detriment are: (a) giving up something that one has a legal right to keep, (b) doing something that one has a legal right not to do, or (c) refraining from doing something that one has a legal right to do.

## Chapter 10 Review

2. Certain acts and promises do not provide consideration. These include a promise to make a gift, a promise to obey the law, or a promise to fulfill an existing duty. In addition, past consideration and illusory promises are not legal consideration.
3. The court usually does not look into the adequacy, or fairness, of consideration. A court may, however, refuse to enforce a contract if the consideration is so inadequate that it is unconscionable.
4. Each promise made as consideration for another promise must create a new obligation. A promise to do something that one is already legally bound to do is not valid consideration.
5. Some promises are enforceable without consideration. These include pledges and subscriptions to charities and promissory estoppel.



### Language of the Law

Choose the term from the list that best completes each sentence below. Then write the complete sentence on a separate sheet of paper.

consideration	gift	illusory
forbearance	benefit	gratuitous
promissory estoppel	unconscionable	detriment

1. One part of consideration is the \_\_\_\_\_, which is something that a party was not previously entitled to receive.
2. A(n) \_\_\_\_\_ is given freely, for no consideration.
3. In a(n) \_\_\_\_\_ contract, an obligation that appears to be binding is not.
4. One part of consideration is the \_\_\_\_\_, which is a type of loss suffered by a party to the contract.
5. \_\_\_\_\_ is not doing something that one has a legal right to do.
6. The exchange of benefits and detriments by the parties involved in a contract is \_\_\_\_\_.
7. Under the doctrine of \_\_\_\_\_, a person who makes a promise must fulfill that promise if failure to do so would be a severe disadvantage to the party to whom the promise was made.
8. When consideration is so inadequate that it shocks the conscience of the court, the contract is \_\_\_\_\_.
9. If there is no consideration, the agreement is \_\_\_\_\_ and the law will not enforce it.



### Questions for Review

Answer the following questions. Refer to the chapter for additional reinforcement.

1. What is consideration?
2. Why is the promise of a gift not enforceable? What is the legal status of a gift that has already been given?

## Chapter 10 Review

3. Will the courts enforce a contract that is based on past consideration? Explain.
4. Do the courts enforce social agreements? Why or why not?
5. Do courts ordinarily base enforcement of a contract on whether the contract is fair? Explain.
6. What may a court do if it finds a contract to be unconscionable?
7. What kinds of promises are enforceable without consideration? How can this be?
8. What three conditions must be met before the principle of promissory estoppel can be applied?
9. Must the full amount of a debt be paid if the person owed the money agrees to a lesser amount?



### Applying Critical Thinking Skills

Apply your understanding of the chapter concepts by answering the questions below.

1. Is your telephone pledge for a charitable contribution enforceable? Explain.
2. Give an example of forbearance.
3. Past consideration is no consideration. What does this statement mean?
4. Suppose you find a student who has a notebook you want and say, "I'll give you \$20 for that notebook." If the student accepts your offer, is the contract binding? Explain.
5. Under what circumstances might a court not enforce an agreement that contains all the necessary elements of a contract?



### Applying Math Skills

Sue offers Chuck \$250 in consideration for his complete sets of baseball cards for the seven years from 1984 through 1990. Chuck originally paid \$19 each for the 1984 through 1986 sets and \$21 each for the 1987 through 1990 sets. If Chuck accepts Sue's offer, how much profit will he make?



### Cases in Point

For each of the following cases, give your decision and state a legal principle that applies:

1. Horace Kushner was injured in an accident with Vic Ling. Kushner promises not to sue if Ling promises to pay \$1,000. Ling agrees. Is Ling legally bound to his promise?
2. Tammy Carson's car runs out of gas. Ned Grover, driving by, sees Carson and offers to tow her car to the next service station. Carson accepts the offer. After they reach the service station, Carson tells Grover she will send him a check for \$25 for his kindness. Is she legally bound to do so?
3. Lisa Lowe takes her car to the Browning Garage and agrees to pay \$75 for a tune-up. Before the job is completed, Lowe tells the owner, "I'll pay you \$10 extra if you do a good job." Is Lowe bound to her promise?