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Contracts—1964 Tennessee Survey

*Paul J. Hartman**

I. Promissory Estoppel—Application by Federal Court

One of the questions presented to the Sixth Circuit Court of Appeals in the case of *Pitts v. McGraw Edison Co.*,[1] was whether the doctrine of promissory estoppel should be recognized and applied by the federal court as the law of Tennessee.

Plaintiff was for many years a manufacturer's representative for defendant. During this time, plaintiff was free to represent other manufacturers, his status being that of an independent contractor, and the agreement was terminable without notice at the will of either party. In 1955, the defendant informed the plaintiff by letter that he was to be retired as defendant's sales representative. In this letter defendant informed the plaintiff that he would pay him a one per cent override commission on sales in the area by the new representative, to wit, "you will get your check each month just as you have been in the habit of getting your check on commissions."[2] Plaintiff was not required to perform any services for the payments. The defendant merely requested, in the nature of a favor solicitation, that the plaintiff aid defendant's new sales representative in whatever manner he could. After payment of the monthly commission for five years, the defendant ceased payments, and following an unsuccessful protest, the plaintiff brought suit.

Plaintiff's first theory was that of ordinary contract, *viz*, that the

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1. 329 F.2d 412 (6th Cir. 1964).
2. *Id.* at 414.

defendant's letter informing him of the monthly payments and asking him to help the new representative was an offer, which was accepted by his giving assistance to the new representative. The district court disposed of this theory by noting that there was nothing which the plaintiff was required to do; hence, there was no valid consideration to support a contract. The appellate court agreed. It might be pointed out in passing, however, that a binding unilateral contract never requires the promisee (plaintiff here) to obligate himself by a return promise to do anything. Nevertheless, the promisor is contractually bound.

Plaintiff's alternative theory was based on the doctrine of promissory estoppel. Using the *Restatement* definition of promissory estoppel,[3] the court pointed out that the doctrine has had limited application in the United States,[4] and further noted that it was aware of no cases in which the principle had been recognized or applied in Tennessee.[5]

Under the facts of this case, the court did not find the requisite elements of estoppel necessary to enforce defendant's promise. The opinion further noted that although there were possibly other factors which would prevent the case from coming within the scope of *Restatement* section 90, the important fact was that plaintiff had not altered his position in reliance on defendant's promise of monthly payments. The court noted that the plaintiff did not give up anything to which he was legally entitled, and that he in no way restricted his activities in exchange for the payments. The conclusion was that the injustice required under *Restatement* section 90 to enforce the promise was not present.

Had there been substantial forbearance by the plaintiff in this case, the promissory estoppel doctrine might have been applicable. For example, if the plaintiff had given up other offers of employment on the strength of defendant's promise of the commission payments,[6] or, if it were a situation where the plaintiff had remained in defendant's employ in reliance upon future payments,[7] the facts might well have brought the case within section 90 of the *Restatement*. Even

3. RESTATEMENT, CONTRACTS § 90 (1932), provides: "A promise which the promisor should reasonably expect to induce action or forbearance of a definite and substantial character on the part of the promisee and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise." For a discussion of promissory estoppel generally, see 1A CORBIN, CONTRACTS §§ 194, 200, 204 (1950); 1 WILLISTON, CONTRACTS § 140 (3d ed. 1957).

4. Annot., 48 A.L.R.2d 1069, 1081, 1085 (1956).

5. Barnes v. Boyd, 18 Tenn. App. 55, 72 S.W.2d 573 (1934). For an earlier discussion of Tennessee's non-recognition of the promissory estoppel doctrine, see 23 TENN. L. REV. 423 (1954).

6. Hunter v. Sparling, 87 Cal. App. 2d 711, 197 P.2d 807 (1948).

7. West v. Hunt Foods Inc., 101 Cal. App. 2d 597, 225 P.2d 978 (1951).

if such additional facts had been present, however, the question remains whether the court would have been justified in applying the promissory estoppel doctrine in this case. The court admitted that it knew of no Tennessee authority for application of the doctrine. Yet, the opinion intimates that had the requisite elements of *Restatement* section 90 been present, the defendant's promise would have been enforced. It seems, however, that the court should have determined, if it could, whether Tennessee applies promissory estoppel, since it is the duty of the federal court to apply the existing state substantive law.

II. Third Party Beneficiary—Enforcement of Labor and Material Bond

National Surety Corp. v. Fischer Steel Corp.,[8] raised the question of whether a third party beneficiary to a labor and material bond could enforce provisions of the bond which were broader than the statutory requirements.

Plaintiff was an unpaid materialman who had supplied materials to a contractor, the principal on the bond. The bond required written notice of claim within ninety days only if the claimant did not have direct contact with the principal; further, it provided that an action could be brought within one year after the principal ceased work under the contract. Finally, the bond provided that "if any limitation embodied in this bond is prohibited by any law controlling the construction hereof such limitation shall be deemed to be amended so as to be equal to the minimum period of limitation permitted by such law."[9]

Under the Tennessee statutes, notice within ninety days is required of a materialman claiming under such a surety bond,[10] and the action must be brought within six months following completion of the work.[11]

Plaintiff gave no notice and his action was not brought within six months as required by statute, although the action was commenced within one year following the work's completion. Defendant maintained that the plaintiff was subject to the statutory provisions and was given no independent rights under the bond. The court, however, did think that plaintiff derived independent rights from the bond in that, under its terms, no notice was required of those of plaintiff's status and there was a stipulation of a one year period during which

8. 374 S.W.2d 372 (Tenn. 1964).
9. *Id.* at 374.
10. Tenn. Code Ann. § 12-421 (1955).
11. Tenn. Code Ann. § 12-422 (1955).

action could be brought. The court reasoned that the bond did not refer specifically to the statutes nor did it make the statutory provisions a part of the bond's conditions.

Third party beneficiary contracts are recognized and enforced in Tennessee.[12] This position is in accord with the *Restatement of Security*[13] as well as the almost universal view.[14] Moreover, provisions in a bond which go beyond the statutory requirements constitute a valid common law undertaking of the surety,[15] and "a bond . . . is good at common law if entered into voluntarily and for valid consideration, and if it is not repugnant to law or the policy of the law, the surety is bound according to its terms."[16]

The bond sued upon, then, expressly gave rights beyond minimum statutory requirements and,

> Where a statute requires that the contractor for a public improvement shall 'give a bond conditioned for the payment of labor and materials, the bond may be conditioned more broadly than the statute requires, and if a bond so conditioned is voluntarily given in consideration of the contract, its extra-statutory provisions may be enforced as a common law obligation.'

The statute merely states minimum requirements.[17]

Cases on which defendant relied as being contrary were readily distinguished in that by the terms of the bonds involved, the bonds were limited to the language of the statutes.[18]

Defendant also contended that the language of this bond limited its terms to the minimum statutory requirements.[19] The court concluded, however, that this provision referred to a situation where the contractual period was less than the minimum required by statute and, since the bond expressly privided for the one year limitation, such limitation was to be changed only if prohibited by law. Since no law prohibited the longer period, the terms of the bond created a common law obligation enforceable against the defendant.

Since statutory provisions for public bonds are a minimum standard required for the public good, there is no reason why the parties

12. Associated Indem. Corp. v. McAlexander, 168 Tenn. 424, 79 S.W.2d 556 (1935); Peoples Bank v. Baxter, 201 Tenn. 283, 298 S.W.2d 732 (1956).

13. RESTATEMENT, SECURITY § 165 (1941).

14. 2 WILLISTON, *op. cit. supra* note 3, § 372.

15. Standard Oil Co. v. Jamison Bros., 166 Tenn. 53, 59 S.W.2d 522 (1933).

16. Day v. Walton, 199 Tenn. 10, 22, 281 S.W.2d 685, 691 (1955).

17. Hogan v. Walsh & Wells, Inc., 180 Tenn. 670, 671, 177 S.W.2d 835, 836 (1944). See also Clatsop Cy. *ex rel.* Hildebrand v. Feldschau, 101 Ore. 369, 199 Pac. 953 (1921). See discussion in 43 AM. JUR. *Public Works and Contracts* § 146 (1942).

18. City of Knoxville v. Burgess, 180 Tenn. 412, 175 S.W.2d 548 (1943); Cass v. Smith, 146 Tenn. 218, 240 S.W. 778 (1922); City of Bristol v. Bostwick, 139 Tenn. 304, 202 S.W. 61 (1918).

19. See text accompanying note 9 *supra*.

contracting among themselves should not be able to extend these minimum requirements. The court's decision seems based on sound precedent.

III. Statute of Frauds—Statute as Defense to Third Party

Love & Amos Coal Co. v. UMW[20] contains interesting dictum on the question of whether a person being sued for inducing breach of an oral contract unenforceable under the statute of frauds may rely on the statute as a defense.

Love & Amos, a coal broker, entered into an oral contract with Osborne Mining Company whereby Osborne agreed to supply coal to Love & Amos for a period of two years. Osborne did not employ union help. Through harassment, violence, and threats, the United Mine Workers caused Osborne to shut down its plant, rendering it unable to perform its contract with the plaintiff. In an action by Love & Amos against United Mine Workers for inducing breach of contract, the Davidson County Circuit Court awarded actual as well as treble damages under Tennessee's Treble Damage Statute.[21]

The defendant, relying on *Evans v. Mayberry*[22] and *Watts v. Warner*,[23] claimed that since the contract between plaintiff and Osborne was unenforceable under the statute of frauds, it could not be held liable for inducing the breach of that contract. The court rejected defendant's argument, and distinguished these cases by noting that in both of them the breaching party had repudiated the contract; whereas, in the instant case, the parties to the contract had reaffirmed the agreement and had continued their efforts to comply with it. The court quoted from the *Watts* case, noting that the rule had been reiterated in the *Evans* case:

> No judgment could be based against a defendant for interference with an unenforceable repudiated contract. Certainly after repudiation there were no legal rights under such a contract which could be infringed.

The court thought that the rule stated in those opinions[24] should not be extended beyond their facts.

It should be noted that in the case at hand the defendant did not specially plead the statute of frauds as required under Tennessee law.[25]

20. 378 S.W.2d 430 (Tenn. App. M.S. 1964).
21. Tenn. Code Ann. § 47-1706 (Supp. 1964).
22. 198 Tenn. 187, 278 S.W.2d 691 (1955).
23. 151 Tenn. 421, 269 S.W. 913 (1925).
24. *Id.* at 422, 269 S.W. at 914.
25. Tenn. Code Ann. § 23-201 (1955). That the statute of frauds normally must be specially pleaded, see 2 Corbin, *op. cit. supra* note 3, §§ 317-20. See also 49 Am. Jur. *Statute of Frauds* §§ 601, 602 (1943).

Further, in the instant case, the court indicated that even had the statute been specially pleaded, the memorandum requirement of the statute of frauds was satisfied by way of a collateral writing in which the contract between plaintiff and Osborne was specifically mentioned.[26]

The majority view is that the statute of frauds is available as a defense only to parties to the contract and those in privity with them.[27] Tennessee, however, has adhered to the minority view that the statute may be used defensively by third parties.[28] An interesting aspect of the instant case is in the court's language that the rule of the *Watts* and *Evans* cases should be restricted to their facts; thus, it appears that the opinion may reflect a possible retreat from the minority view. The court seems to say that even if the writing requirement had not been satisfied and the statute had been specially pleaded, the decision in this case would have been the same. In distinguishing the instant case from *Watts* and *Evans*, it was emphasized that in these two decisions, the contracts had been repudiated, and there were, therefore, no legal rights to be infringed. This distinction is perhaps but a convenient way for the court to begin its retreat from Tennessee's previous minority position. At least in a suit for inducing breach where the party had been induced to repudiate the contract by the defendant, rather than to fail in performance, the court's reasoning would seem to be a distinction without a difference, unless the contract had been repudiated absent any inducement by the defendant.

The purpose of the statute of frauds is not to render recognized contracts unenforceable but to prevent fraud.[29] The statute should not, therefore, be available to enable a wrongdoer to escape liability for his wrongful conduct through a mere technicality.

IV. PAROL EVIDENCE RULE—APPLICATION TO EXTRINSIC SUBSEQUENT AGREEMENT

Trice v. Hewgley[30] applied the rule that the establishment by parol evidence of an agreement made subsequent to the writing is

26. 378 S.W.2d at 430, 438, 439.

27. 2 CORBIN *op. cit. supra* note 3, § 289; 2 WILLISTON, CONTRACTS § 530 (rev. ed. 1936). See Annot., 26 A.L.R.2d 1227 (1952); Annot., 84 A.L.R. 43 (1933). See also RESTATEMENT, CONTRACTS § 218 (1932). Note that illustration 1 of this section is particularly applicable to the instant case.

28. Elsewhere the writer has had occasion to criticize the minority position taken by Tennessee. See Hartman, *Contracts—1955 Tennessee Survey*, 9 VAND. L. REV. 951, 958 (1956).

29. 2 Corbin, *op. cit. supra* note 3, §§ 317-20.

30. 381 S.W.2d 589 (Tenn. App. M.S. 1964).

not prohibited by the parol evidence rule.[31]

Plaintiff, as executrix of deceased's estate, sued defendant on several promissory notes owed by defendant to the deceased. By way of defense, defendant alleged that a certain amount of the indebtedness had been forgiven. The basis of the defense was an oral agreement in which defendant had agreed to convey to the deceased certain mill property, in return for which the deceased was to have conveyed a parcel of land and to have forgiven the amount of the indebtedness in question. Plaintiff maintained that the parol evidence rule prevented the defendant from proving the agreement and, hence, the amount of the debt which was forgiven.

The court sustained defendant's position, and in stating the majority and Tennessee rule,[32] quoted from *Brunson v. Gladish*, that the parol evidence rule:

> does not prohibit the establishment by parol evidence of an agreement made subsequent to the execution of the writing, although such subsequent agreement may have the effect of adding to, changing, modifying or even altogether abrogating the contract of the parties as evidenced by the writing; for the parol evidence rule does not in any way deny that the original agreement of the parties was that which the writing purports to express, but merely goes to show that the parties have exercised their right to change or abrogate the same, or to make a new and independent contract.[33]

This clearly is a correct interpretation of the parol evidence rule which applies only to extrinsic agreements made prior to or contemporary with the written agreement in question. No further citation of authority is needed to support this proposition of law.

V. Illegal Bargains—Agreement Not to Compete

Federated Mutual Implement & Hardware Insurance Co. v. Johnson[34] held as reasonable an employment contract in which the defendant employee had agreed not to compete with the plaintiff employer in a territory, consisting of several counties, for a period of two years after defendant's termination of employment.

The defendant violated this agreement and the plaintiff brought action for an injunction and for damages. The chancellor dissolved the temporary injunction which he had issued, dismissed the case

31. For the rule, see generally Restatement, Contracts §§ 237-44 (1932); 4 Williston, *op. cit. supra* note 3, §§ 631, 632.

32. The general rule is stated in Williston, *op. cit. supra* note 3, § 632. For application of the rule in Tennessee, see Goodwin v. Goodwin, 36 Tenn. App. 630, 260 S.W.2d 186 (M.S. 1953); Perry v. Central R. Co., 45 Tenn. 138 (1867).

33. Brunson v. Gladish, 174 Tenn. 309, 316, 125 S.W.2d 144, 147 (1939).

34. 382 S.W.2d 214 (Tenn. App. W.S. 1964).

and plaintiff appealed. The court of appeals sustained the plaintiff.

The case is practically on all fours with *Federated Mutual Implement & Hardware Insurance Co. v. Anderson*,[35] which involved a contract almost identical to the agreement in the instant case. The only difference was that in *Anderson* there was no stipulation for liquidated damages and the territory comprised a larger area. Yet, the Court of Appeals for the Eastern Section had reversed a dismissal of the bill by the chancellor.[36] The chancellor in the instant case, however did not think the *Anderson* case controlling on the facts. In disagreeing with the chancellor the *Johnson* court quoted the *Anderson* case as follows:

> Contracts to protect an employer by restriction of subsequent employment of the employee within reasonable lengths of time and space are permitted and sanctioned and equity will enjoin an employee from competing in violation of the restrictive provisions of his employment contract.[37]

The reasons for upholding such a contract was explained in the case of *Arkansas Dailies v. Dan*:

> A business is built upon the confidence of its customers and the employee gains acquaintances and sells the customers by using the good will of the employer. The employer's dealings with the customer through the employee gives the employee confidential knowledge that should not be divulged or used for his own benefit. . . .[38]

Restrictive contracts, such as the one involved in the instant case are upheld when they are reasonable as to time and space.[39] The facts of the case before the court fall clearly within the *Restatement* provision as an instance of a reasonable restraint:

> A bargain by an assistant, servant, or agent not to compete with his employer, or principal, during the term of the employment or agency, or thereafter within such territory and during such time as may be reasonably necessary for the protection of the employer or principal, without imposing undue hardship on the employee or agent.[40]

This provision is well recognized in Tennessee.[41]

35. 49 Tenn. App. 124, 351 S.W.2d 411 (E.S. 1961).
36. Ibid.
37. *Id.* at 133, 351 S.W.2d at 415.
38. 36 Tenn. App. 663, 673, 260 S.W.2d 200, 204 (W.D. 1953).
39. On two earlier occasions the writer has had occasion to discuss the validity of agreements in restraint of trade in Tennessee. See Hartman, *Contracts—1961 Tennessee Survey*, 14 VAND. L. REV. 1196, 1212 (1961); Hartman, *Contracts—1957 Tennessee Survey*, 10 VAND. L. REV. 1013, 1033 (1957). For instances where restrictive contracts have been held unenforceable, see Annot., 3 A.L.R.2d 519 (1943). See also 36 AM. JUR. *Monopolies* §§ 50, 54 (1941).
40. RESTATEMENT, CONTRACTS § 516 (1932).
41. Matthews v. Barnes, 155 Tenn. 110, 293 S.W. 993 (1927); Turner v. Abbott,

VI. Death of Party to Personal Service Contract as Terminating the Contract

Rodgers v. Southern Newspapers Inc.[42] raised the question of when the death of one of the parties to a personal service contract will terminate the agreement.

Plaintiff's husband sold a newspaper to defendants in 1946. At that time, he entered into a contract with defendants whereby he was to receive monthly payments for twelve years in return for his services as director and consultant of the newspaper. After his marriage to plaintiff in 1955, Mr. Rodgers, plaintiff, and defendant entered into a separate contract. This agreement provided that upon expiration of the twelve year contract, or upon its termination, there would be a continuation of the original agreement for a period of ten years, with a provision for monthly payments to Mr. Rodgers for his services. In addition, the agreement provided the following:

> Should party of the first part die before the ending of the term of payments provided for in this contract then the remaining payments shall be made to his wife, Della Richard Rodgers, and in such event she shall substitute in the service agreed to herein and be paid for such remaining period.[43]

Plaintiff's husband died in 1957, with about a year left to run on the original agreement. Defendant refused to allow Mrs. Rodgers to substitute her performance under the contract on the theory that the agreement terminated by Mr. Rodgers' death. Plaintiff's suit in chancery court was dismissed and she appealed.

The court recognized the well established general rule that in a personal service contract, death of one of the contracting parties generally terminates the agreement.[44] There are exceptions to the general rule, however, *e.g.*, when the service is of such character that it can be performed by another or when the contract's terms show that performance by others was contemplated.[45] The court noted that it had previously recognized such exceptions,[46] and also took cognizance of the *Restatement* view that a party is not discharged by death if the

116 Tenn. 718, 94 S.W. 64 (1906); Arkansas Dailies v. Dan, 36 Tenn. App. 663, 260 S.W.2d 200 (W.D. 1953).

42. 379 S.W.2d 797 (Tenn. 1964).

43. *Id.* at 798.

44. 6 Williston, *op. cit. supra* note 27, § 1940. For a discussion of the general rule see 17 Am. Jur. 2d *Contracts* § 413 (1964).

45. *Ibid.* See also Restatement, Contracts § 459 (1932).

46. Greenwood v. National Biscuit Co., 175 Tenn. 302, 134 S.W.2d 149 (1939). For other cases recognizing the exception, see Howard v. Adams, 16 Cal. 2d 253, 105 P.2d 971 (1940); Stein v. Bruce, 366 S.W.2d 732 (Mo. App. 1963); McCarty v. Sturm, 289 P.2d 145 (Okla. 1954).

contract indicates a contrary intention.[47] The court thought it clear that under the terms of the contract the parties had contemplated substitution of plaintiff's services in the event of Mr. Rodger's death and, hence, the contract was distinctly within one of the exceptions to the general rule.

The defendant also contended that the ten year contract had not yet begun at the time of Mr. Rodgers' death but the court ruled that there was an executory contract created at the time of the agreement between plaintiff, defendant, and Mr. Rodgers, even though performance was to begin at a future date.

The court's decision seems merely to reflect an application of the well settled rule that a personal service contract need not be terminated by death of one of the parties if performance by another is contemplated and if the parties contract for such substituted performance. The contract here clearly indicates that the parties anticipated the death of Mr. Rodgers and made provision therefor. Moreover, plaintiff was a party to the contract here and had assented to its terms. Since plaintiff had bound herself to the contract's terms it seems clear that defendant could have maintained an action against plaintiff if she had refused to perform after her husband's death.

47. RESTATEMENT, CONTRACTS § 459 (1932).