Vanderbilt Law Review

Volume 17
Issue 3 *Issue 3 - June 1964*

Article 15

6-1964

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Recommended Citation
Paul J. Hartman, Contracts -- 1963 Tennessee Survey, 17 *Vanderbilt Law Review* 962 (1964)
Available at: https://scholarship.law.vanderbilt.edu/vlr/vol17/iss3/15

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Contracts—1963 Tennessee Survey

Paul J. Hartman[*]

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I. Statute of Frauds

Both the one year provision and the sale of goods provision of the Statute of Frauds were construed in *Anderson-Gregory Co. v. Lea.*[1]

Regarding the duration of the contract, the facts in the opinion are somewhat sparse. The plaintiff had orally agreed to furnish to the defendant certain equipment for the transportation and production of gravel, and to supervise the removing of gravel from a pit. When sued for breach of contract, one defense interposed was the one year provision of the Statute of Frauds. Tennessee, in common with most states, has a statute providing, in part, that no action shall be brought:

> Upon any agreement or contract which is not to be performed within the space of one (1) year from the making thereof; unless the promise or agreement, upon which such action shall be brought, or some memorandum or note thereof, shall be in writing, and signed by the party to be charged therewith, or some other person by him thereunto lawfully authorized.[2]

The court held that the contract did not come within this provision of the statute. If a contract could have been performed, under its terms, within a year from the time of its making, it is not within the Statute of Frauds, even though it is improbable that the contract would be performed within a year.[3] No facts appear in the court's opinion to indicate that the contract in question could not have been performed, under its terms, within one year from the time of its making. The result of the case in this regard appears clearly correct.

A second defense interposed was the Statute of Frauds applicable to the sale of goods. Thirty-seven states, including Tennessee, have adopted some form of the Statute of Frauds provision of the Uniform Sales Act. The Tennessee statute provides:

> A contract to sell or a sale of any goods or choses in action of the value of five hundred dollars ($500) or upwards shall not be enforceable by action unless the buyer shall accept part of the goods or choses in action so

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1. 370 S.W.2d 934 (Tenn. App. M.S. 1963).
2. Tenn. Code Ann. § 23-201 (1956).
3. See Corbin, 2 Contracts § 444 (1950); 3 Williston, Contracts § 495 (3d ed. 1960).

> contracted to be sold, or sold, and actually receive the same, or give something in earnest to bind the contract, or in part payment, or unless some note or memorandum in writing of the contract or sale be signed by the party to be charged or his agent in that behalf.[4]

Of course, a basic question in resolving the defense of this section is whether the item sold constitutes "goods" within the meaning of the statute, so as to make the oral contract unenforceable. The Uniform Sales Act provides that an item is not within the statute if the goods are to be manufactured by the seller especially for the buyer and are "not suitable for sale to others in the ordinary course of the seller's business."[5] While adopting part of the Uniform Sales Act section the Tennessee legislature did not, for some reason, adopt the foregoing provision describing the type of goods not falling within the statute. Nevertheless, the court in the case at hand applied essentially the same definition of goods as that found in the Uniform Sales Act.

It will be noticed that, under the Uniform Sales Act, items are not within the Statute of Frauds if the goods are "not suitable for sale to others in the ordinary course of the seller's business." That, of course, is a factual determination. However, goods of standard type in the seller's business are within the Statute of Frauds. It does not matter that the reason for making the goods was to fill the buyer's order; the Statute of Frauds is applicable, and an oral contract is unenforceable if the goods will sell in the ordinary course of the seller's business.[6] Even though the goods are made for buyer's special order, if the seller can at little expense change them so that they will be usable in ordinary course in seller's business, the Statute of Frauds is applicable and the oral contract is unenforceable.[7]

It is not possible to tell from the court's opinion in this case whether the personal property items involved in the oral contract constituted goods within the meaning of the Statute of Frauds. To be sure, as the court points out, seller agreed to furnish certain equipment for the transportation and production of gravel to be used by the buyer. But that leaves unanswered the essential question of whether these

4. TENN. CODE ANN. § 47-1204 (1956).

5. UNIFORM SALES ACT § 4(z).

6. Saco-Lowell Shops v. Clinton Mills Co., 277 Fed. 349 (1st Cir. 1921) (cotton mill machinery); Marilyn Shoe Co. v. Martin's Shoe Store, Inc., 253 S.W.2d 18 (Ky. 1952) (shoes made to order for buyer but according to designs and models in use by seller in ordinary course of business); Berman Stores v. Hirsh, 240 N.Y. 209, 148 N.E. 212 (1925) (men's suits of usual sizes and models, with defendant's labels attached but easily removable).

7. Bauer v. Victory Catering Co., 101 N.J.L. 364, 128 Atl. 262 (Ct. Err. & App. 1925) (silverware made with buyer's initial crest stamped thereon, but removable at small expense). See VOLD, SALES 100 (2d ed. 1959); WILLISTON, SALES § 55 (rev. ed. 1948).

goods were suitable for sale to others in the ordinary course of seller's business. If they were so suitable for sale, the Statute of Frauds is applicable and the oral contract is unenforceable, even though the goods were especially produced for the buyer.

It should be pointed out, however, that the recent adoption by Tennessee of the Uniform Commercial Code changes this exception from the Statute of Frauds for goods to be specially manufactured. As provided by the Uniform Commercial Code, adopted in Tennessee, even if the goods are to be specially manufactured for the buyer and are not suitable for resale to others in the ordinary course of the seller's business, the oral contract is not enforceable unless the manufacturer has made either a substantial beginning of the manufacture of the goods or commitments for the procurement of the goods before there is a repudiation of the oral agreement.[8]

II. CONSTRUCTION

The Tennessee Supreme Court case of *Oman Construction Co. v. Tennessee Central Ry.*[9] raises an interesting and somewhat unusual question relative to the rule that several contracts relating to one transaction are to be construed together. The suit grows out of damages sustained in the construction of a sewer under the freight depot of the plaintiff, Tennessee Central Railway Company. The City of Nashville was causing the sewer to be constructed. Defendants Oman Construction Company, McKenzie Construction Company and Goldberg were held liable to plaintiff in the two lower courts. On appeal, the supreme court exonerated Goldberg from liability, holding McKenzie and Oman liable.

In August, 1952, Goldberg (a firm of architects-engineers) was employed by the City of Nashville as engineers in connection with the construction of a sewage collection and disposal system for the city. Under the terms of this contract Goldberg was to review and report on designs for the sewage system and to supervise and inspect the proposed construction work. In short, under Goldberg's contract with the city, the former was to be the supervising engineer of the construction of the sewer system.

Nearly two years later (May, 1954), the City of Nashville entered into a contract with the plaintiff (Tennessee Central Railway), which thereunder gave an easement to the city, its servants, agents and/or contractors to construct, operate and maintain a sewer across plaintiff's premises. This contract also provided that "all expenses in connection with the construction of said sewer, or damage to facilities

8. TENN. CODE ANN. § 47-2-201(3)(a) (1964). For a fuller consideration of the matter, see Bigham, *Tennessee Law and the Sales Article of the Uniform Commercial Code*, 17 VAND. L. REV. 873, 879 (1964).

9. 370 S.W.2d 563 (Tenn. 1963).

of the Railway as a consequence of said construction or operation is to be borne by the City of Nashville, its servants, agents and/or contractors."

In June, 1954, the city entered into a contract with Oman for the construction of the sewer in question. In this contract it was provided that all work was to be done under the supervision of the engineer (Goldberg) and to his satisfaction; Goldberg was to decide all questions as to quality and acceptability of materials, work performed, manner of performance, rate of progress, etc. Oman's contract with the city also made it clear that Oman should be solely responsible for all damage or injury to property of any character resulting from any negligence in the mauner or method of executing the work. It was specifically provided that Oman should be liable for all injury caused by blasting, and that the city should be saved wholly harmless by Oman. Regarding sewers in tunnels, the contract between Oman and the city specifically provided that Oman should be liable for all damages.

In one count of its declaration, plaintiff alleged that all three defendants (Oman, McKenzie and Goldberg) breached the foregoing contracts and that the building and platforms and tracks of plaintiff were caused to sink and were damaged as a result of such breach of contract; and that this damage came within the provisions of the contract of May, 1954, between the city and plaintiff, the obligations of which were assumed by Oman and McKenzie and that it was also within the provisions of the contract between Oman and the city. Plaintiff also alleged that Goldberg was bound by the terms of the contract between the city and plaintiff; that the damage was done by Oman and McKenzie under the supervision of Goldberg; and that Goldberg breached his own contract by permitting the breach of contract by Oman and McKenzie.

A second count of plaintiff's declaration was in tort and based upon alleged acts of negligence. It charged Oman and McKenzie with specific acts of negligence and alleged that Goldberg was negligent in the supervision of the work by allowing and approving the negligent and careless acts of the contractors, Oman and McKenzie. All defendants demurred to the declaration. The demurrers were overruled and all defendants were held liable in a trial of the matter by the lower courts.

On appeal, the supreme court held that Goldberg was not liable to plaintiff. The court could find no provision in Goldberg's contract with the city or in the contract between Oman and the city or in the contract between the plaintiff and the city which expressly provides for any contractual liability on the part of Goldberg to the plaintiff. The city saw fit, said the court, to place solely on Oman the responsi-

bilities undertaken by it in its contract with plaintiff. The court concluded that it was necessary to examine all of the contracts to determine what were the rights and obligations of the respective parties to this litigation. Contracts relating to one transaction are to be construed together. Construing the contracts relied upon in conformity with this rule, the court said that the city's contract with Goldberg is for the benefit of the city alone. It clearly appears, said the court, that all obligations to pay damages or to indemnify the city or restore damaged property are made the obligation of Oman alone and no such obligations are placed upon Goldberg in the contract between Oman and the city.

To be sure, the contract between Oman and the city does not purport to place any obligation upon Goldberg. Indeed, it would be most difficult for the city and Oman by their contract made after Goldberg was hired to saddle Goldberg with an obligation. By the same token, it is difficult to see how plaintiff's claim against Goldberg can be affected by the contract between city and Oman in which Oman agreed to be solely responsible for any damages done in building the sewer. Plaintiff was in no sense a party to the subsequent agreement by which Oman promised the city to assume full liability for any damages done.

After finding that the contract between Goldberg and the city did not give plaintiff any contractual rights against Goldberg, the court held, quite properly it seems, that plaintiff was a third party beneficiary of Oman's contract with the city; hence plaintiff had a cause of action against Oman for breach of contract.[10]

III. SPECIFIC PERFORMANCE

The Tennessee Court of Appeals case of *Turner v. Zager*[11] involves some rather interesting points concerning the specific performance of a contract to sell shares in a close corporation, where the seller retained the right to repurchase the shares, and both parties reserved the right to terminate the agreement on ten days notice.

The defendant-seller, as part of an arrangement whereby plaintiff would continue to work for the Fairfax Corporation, gave plaintiff the option to purchase sixty shares of stock in Fairfax, a close corporation, in which defendant was the principal stockholder. The option was not immediately exercised by plaintiff and defendant, pursuant to a term of the agreement containing the option, notified plaintiff

10. La Mourea v. Rhude, 209 Minn. 53, 295 N.W. 304 (1940). The court sustained Goldberg's demurrer to plaintiff's count in his declaration charging Goldberg in tort, on the ground that the count in tort was improperly joined with the count wherein other defendants were sued in contract.

11. 363 S.W.2d 512 (Tenn. App. M.S. 1962).

that he (defendant) was cancelling the transaction. The agreement provided that it could be terminated by either party with or without cause on ten days notice. Within ten days after plaintiff received the notice of cancellation, he notified defendant that he was prepared to exercise his right to purchase the sixty shares of stock. Defendant refused to deliver the shares, and plaintiff brought suit for specific performance.

The court held that since this was a close corporation, plaintiff was entitled to specific performance, as plaintiff could not buy shares in the corporation elsewhere. The court properly took the position that when defendant granted plaintiff, for a valuable consideration, the option to purchase the shares, that created an irrevocable offer, which, on acceptance in accordance with its terms, gives rise to a contract. The attempted cancellation did not destroy plaintiff's power to exercise the option within ten days after the defendant gave plaintiff notice of the termination. The option given plaintiff by defendant was, itself, a contract to keep an offer open.[12]

By way of defense, defendant also urged that his (defendant's) right to repurchase the shares should defeat plaintiff's remedy. The court refused to accept this argument saying:

> We cannot accept the argument since defendant has the option to repurchase the stock he has the power to negate a decree of specific performance. He has no power to exercise the option unless he, himself, transferred the stock to complainant.
> Defendant cannot negate specific performance because he terminated the contract upon which he must rely for the right to repurchase. Having terminated the contract, there is no contract in existence. If he desired to take advantage of the contract provision permitting him to repurchase, he should have done this upon receiving complainant's acceptance and prior to the termination of the contract in accordance with his own act.[13]

A question or two might be asked regarding the logic of this reasoning. First, how could defendant have exercised his right to repurchase "upon receiving complainant's acceptance and prior to the termination of the contract in accordance with his (defendant's) own act?" Defendant had given his notice of termination ("his own act") before plaintiff had ever exercised his option to purchase the shares. Hence, it was impossible for defendant to have repurchased the shares before plaintiff had purchased them. Does not this reasoning by the court also mean that defendant could not have repurchased the shares, even if he had tried to do so within the ten day cancellation period before termination became effective? The court also says that since defend-

12. See 1 WILLISTON, CONTRACTS §§ 61-61D (3d ed. 1957), for a discussion of the nature of an option and the circumstances making it irrevocable.

13. Turner v. Zager, *supra* note 11, at 518.

ant had terminated the contract, there is no contract in existence. Yet, the court did specifically enforce the contract against defendant. Somehow, a contract of some sort must have remained in existence. Moreover, does not this reasoning defeat one of the purposes of the agreement, which was to permit the defendant to keep this a close corporation?

IV. EXCULPATORY CONTRACTS

Smith v. Southern Bell Telephone and Telegraph Co.[14] presents the question whether a telephone company can, by contracting in advance, limit its future liability for its negligence with respect to advertisements in the classified directory or "yellow pages." The plaintiff had been advertising in the yellow pages of the defendant's telephone directories for a number of years. As part of plaintiff's contract with the defendant telephone company there was a provision limiting defendant's liability for mistakes in the advertising to seventy-five dollars. The advertisement in the "yellow pages" of defendant, placed there by plaintiff, a florist, was in error. As a result of the error, plaintiff claimed substantial damages.

The sole issue was whether this contractual provision limiting defendant's liability is contrary to public policy and, therefore, invalid. The court held that this exculpatory clause in the contract between the parties was valid.

Normally exculpatory contracts by which common carriers and other public service corporations, such as the defendant, undertake to contract away their liability in advance for their negligent conduct will be held against public policy and invalid.[15] Various reasons are given for striking down such exculpatory clauses. One is the inequality of bargaining power of the parties. A carrier of public service company with its monopoly has the power to exact a contract that is most favorable to it; on the other hand, the other party must either agree to relieve the carrier or public service company of liability for its negligence or refuse to agree at the risk of great inconvenience. Too, the incentive to use due care would be destroyed if harm can be inflicted with impunity by a carrier or public service company because of the relieving clause.

However, as the court in the case at hand properly points out, where a common carrier or public utility is not acting in the discharge of its duty as a carrier or utility, it may validly contract against liability for

14. 364 S.W.2d 952 (Tenn. App. W.S. 1962).

15. Fairfax Gas & Supply Co. v. Hadary, 151 F.2d 939 (4th Cir. 1945) (gas company); Pierce v. Southern Pac. Co., 120 Cal. 156, 47 Pac. 874 (1897); Shellabarger Elevator Co. v. Illinois C.R.R., 278 Ill. 333, 116 N.E. 170 (1917); Turner v. Southern Power Co., 154 N.C. 131, 69 S.E. 767 (1910) (electric company); 6 WILLISTON, CONTRACTS § 1751C (3d ed. 1957); Annot., 175 A.L.R. 8, 38-39 (1948).

its future negligent conduct.[16] Southern Bell presumably is not acting in the discharge of its duty as a utility by printing plaintiff's advertisements in Southern Bell's "yellow pages." Tested by the criteria usually employed by the courts in determining the validity of contractual clauses relieving against liability for the consequences of negligence, the exculpatory clause in the *Southern Bell* case would be sustained. However, there still remains a rather forceful argument against the validity of such exculpatory clauses. The incentive to use due and reasonable care is, in part, destroyed. The party knows that he has been given an immunity bath from liability for the consequences of his negligence through the contract, which has insulated him from the payment of damages for future injury suffered by the other party.[17]

16. Baltimore & O.S.R.R. v. Voigt, 176 U.S. 498 (1899); see Ringling Bros.-Barnum & Bailey Combined Shows v. Olivera, 119 F.2d 584, 587 (9th Cir. 1941).

17. Elsewhere the writer has discussed exculpatory contracts in considerably more detail. See Hartman, *Tennessee Survey 1960—Contracts,* 14 VAND. L. REV. 1207 (1961). Minton v. General Shale Prod. Corp., 371 S.W.2d 808 (Tenn. App. E.S. 1962), involves a question bearing on an illegal agreement. There the court concluded that, for reasons of policy, agreements between shippers and motor carriers for the payment of rates varying from those provided in the tariffs or schedules of charges filed with the Interstate Commerce Commission cannot be recognized nor allowed, nor can any act or omission of the carrier be permitted to estop it from forcing payment of the full amount of such transportation charges.