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RECENT DEVELOPMENTS IN NORTH DAKOTA CONTRACT LAW

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I. INTRODUCTION

This Article was originally intended to be a survey of all the contract cases heard by the North Dakota Supreme Court during the period from 1980 through 1983. The initial research, however, revealed that the North Dakota Supreme Court heard an unmanageably large number of contract cases during that time period. Although it is interesting to note the vitality of contract law in North Dakota, it became necessary to limit the scope of this Article to a manageable size. The survey period, therefore, was limited to cases heard by the court between January 1982 and June 1983 and includes only those contract cases that are of interest to the North Dakota attorney. These cases are the subject of this Article.

The largest number of cases that the court heard during the survey period covered issues regarding the interpretation of contracts.[1] The court also heard a substantial number of cases that

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1. *See, e.g.*, Oakes Farming Ass'n v. Martinson Bros., 318 N.W.2d 897 (N.D. 1982) (discusses general rules of contract interpretation). See *infra* notes 44-144 and accompanying text for a discussion of a variety of interpretation issues.

dealt with damages issues[2] and estoppel.[3] The number of cases in these categories alone tells a story: contract law in North Dakota is becoming increasingly flexible. For example, in the interpretation area, the court appears to evidence an increased willingness to look beyond the four corners of a written document both to ascertain whether a latent ambiguity might exist and to ascertain the meaning of an ambiguity. Similarly, the court has been increasingly willing to recognize promissory estoppel or reliance, both as a substitute for consideration and as a device to estop one party from taking undue advantage of another in the contract context. The court has also recognized that as it increased its willingness to look beyond the four corners of the contract, for the sake of achieving a fair result on the facts of a particular case, it was necessary to use more flexibility in remedial matters. For example, while the court increased its recognition that some relief should be given in the case of quasi-contracts[4] or when a party has justifiably relied upon the actions of another party to its detriment,[5] the court has been attentive to the need to moderate the remedial portion of its decisions, giving relief in the form of restitution, reliance, or in some manner that deviates from the conventional expectation measure of damages.

Thus, during the period covered in this Article, the North Dakota Supreme Court has increasingly evidenced a willingness to apply contract doctrines in a flexible manner. Nevertheless, a tension is developing in the case law because the court often asserts a basic fidelity to the freedom of contract and to certainty in contractual relationships as well, particularly in contexts when the parties are endowed with essentially equal bargaining power.

This tension, which characterizes much of the contemporary contract law, surfaces occasionally in the North Dakota cases covered in the survey period but its ultimate resolution is far from

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2. *See* Hall GMC, Inc. v. Crane Carrier Co., 332 N.W.2d 54 (N.D. 1983) (computation and allowance of special damages); Storebo v. Foss, 325 N.W.2d 223 (N.D. 1982) (measure of damages in a breached construction contract); Kulseth v. Rotenberger, 320 N.W.2d 920 (N.D. 1982) (damages recoverable when basing an action in *quantum meruit*); Hofmann v. Stroller, 320 N.W.2d 786 (N.D. 1982) (distinction between incidental and consequential damages); Hirschkorn v. Severson, 319 N.W.2d 475 (N.D. 1982) (allowable interest as an element of damages). See *infra* notes 170-99 and accompanying text for a discussion of damage issues.

3. *See, e.g.*, O'Connell v. Entertainment Enter., 317 N.W.2d 385 (N.D. 1982) (discusses the elements of equitable and promissory estoppel). See *infra* notes 19-43 and accompanying text for a discussion of equitable and promissory estoppel and other reliance issues.

4. *See, e.g.*, Jerry Harmon Motors, Inc. v. Heth, 316 N.W.2d 324 (N.D. 1982) (court allowed recovery for the partial cost of a four-wheel drive conversion kit on the theory of quasi-contract or unjust enrichment). See *infra* notes 112-23 and accompanying text for a discussion of *Heth*.

5. *See, e.g.*, O'Connell v. Entertainment Enter., 317 N.W.2d 385 (N.D. 1982) (discussion of the elements of equitable and promissory estoppel). See *infra* notes 19-43 and accompanying text for a discussion of estoppel, reliance, and other related issues.

certain. Thus, while this Article is not intended to indicate how this tension is or should be resolved, it is important for the practitioner to be aware of this tension and its potential ramifications in North Dakota.

The remainder of this Article discusses the cases covered in the survey period. The cases are divided into categories by issues. The first category of cases discusses issues relating to the formation of a contract. Second, this Article will discuss general and specific interpretation issues. The third category of cases examines contract defenses. Fourth, this Article will discuss remedial issues. Finally, this Article will examine miscellaneous issues relating to contract law.

Given the broad scope of this Article, it can be little more than a helpful introduction to contemporary contract law in North Dakota. Hopefully, this Article will at least fulfill this limited purpose in a manner beneficial to practitioners.

II. FORMATION

A. CONSIDERATION

1. E.E.E., Inc. v. Hanson

In *E.E.E., Inc. v. Hanson*[6] the defendant executed a mortgage to obtain bank financing for a laundromat.[7] Unfortunately, the bank refused to make the loan.[8] The trial court concluded that the mortgage was unenforceable since the primary consideration for the mortgage, the bank loan, had failed.[9] The supreme court, however, ruled that although the primary consideration had failed, other good and sufficient consideration existed.[10] This consideration was a preexisting debt that Hanson owed to the mortgagee, E.E.E., Inc.[11] The supreme court reasoned that if there

6. 318 N.W.2d 101 (N.D. 1982).

7. E.E.E., Inc. v. Hanson, 318 N.W.2d 101, 106 (N.D. 1982). E.E.E. was building a laundromat for Hanson. *Id.* In December 1979 Hanson signed a promissory note payable to E.E.E. in the amount of $66,233. *Id.* On February 4, 1980, Hanson executed two mortgages in favor of E.E.E. *Id.* The first mortgage covered the laundromat and the second mortgage covered certain farmland in Griggs County. *Id.* The mortgages were assigned to Page State Bank to allow Hanson to obtain financing for the laundromat. *Id.* The bank discovered that the land was previously mortgaged and declined to make the loan. *Id.*

8. The previous mortgage on the property was $83,200 in favor of Hanson's heirs. *Id.*

9. *Id.* at 107. Another reason why the trial court decided that the mortgage was a nullity was that the promissory note on which the mortgage was based did not contain language of unconditional promise. *Id.* at 106.

10. *Id.* at 107. *See* A. CORBIN, CORBIN ON CONTRACTS § 126 (1963). Professor Corbin indicates that if two considerations exist for a promise, one of which is legally sufficient while the other is not, the promise is enforceable based upon the legally sufficient consideration. *Id.*

11. 318 N.W.2d at 107. A preexisting debt is good consideration for a mortgage. Sargent v. Cooley & Clifford, 12 N.D. 1, 5, 94 N.W. 576, 577 (1902).

are several considerations and some fail, if the others are good and sufficient, the good will sustain the promise.[12] This case clearly illustrates the lengths to which the court will go to find additional consideration, even when the primary consideration in a transaction fails.

Apparently, with the court's holding in *Hanson*, if the parties intend for the agreement to be void if the *primary* consideration fails, the parties must express this intention within the agreement. The wise drafter would do well to specify the consideration contemplated by the contracting parties and the precise effect a failure of that specific consideration would have on the agreement.

2. *Pioneer Credit Co. v. Medalen*

The defendant in *Pioneer Credit Co. v. Medalen*[13] signed a guarantee of payment that clearly stated the consideration for the guarantee was Pioneer Credit's promise to withhold execution on a judgment against Medalen's daughter and son-in-law.[14] When the daughter and son-in-law filed for bankruptcy, Pioneer Credit sought payment from Medalen.[15] Medalen argued that the guarantee was not supported by sufficient consideration.[16] The Supreme Court of North Dakota found that Pioneer Credit had given adequate consideration.[17] As the court concluded, "Surrender of a legal right or forbearance constitutes valid consideration."[18]

B. ESTOPPEL: EQUITABLE AND PROMISSORY

1. *O'Connell v. Entertainment Enterprises*

Evaluating the plaintiff's equitable estoppel claim, the court in *O'Connell v. Entertainment Enterprises*[19] cited section 31-11-06 of the

12. 318 N.W.2d at 107.

13. 326 N.W.2d 717 (N.D. 1982).

14. Pioneer Credit Co. v. Medalen, 326 N.W.2d 717, 719 (N.D. 1982).

15. *Id.* at 718. Pioneer filed suit against Medalen for payment under the guarantee of payment. *Id.* Medalen initially did not answer the complaint. *Id.* At the hearing the court granted Medalen a ten day extension. *Id.* After a second hearing, the court entered a summary judgment in favor of Pioneer. *Id.*

16. *Id.* at 719. Medalen also unsuccessfully argued that he should not be held liable because he did not read the guarantee of payment and because his signature was fraudulently obtained. *Id.* His supporting affidavits in opposition to the summary judgment motion, however, failed to establish either allegation. *Id.*

17. *Id.* Surrender of a valid legal right is good consideration. *Id.* Pioneer surrendered the legal right to execute on a judgment. *Id.* at 718.

18. *Id.*

19. 317 N.W.2d 385 (N.D. 1982). O'Connell was the manager of the Crown Colony Entertainment Center in Grand Forks from January 1977 through August 1981. O'Connell v.

North Dakota Century Code,[20] which codifies the doctrine, and *Farmers Cooperative Association of Churchs Ferry v. Cole*,[21] which sets forth the elements of the doctrine. The court stated,

> [T]he basic elements of an equitable estoppel, insofar as it relates to the person being estopped, are: (1) conduct which amounts to a false representation or concealment of material facts, or, at least, which is calculated to convey the impression that the facts are otherwise than those which the party subsequently attempts to assert; (2) the intention, or at least the expectation, that such conduct will be acted upon by, or will influence, the other party or persons; and (3) knowledge, actual or constructive, of the real facts. Insofar as related to the party claiming the estoppel, the elements are: (1) lack of knowledge and of the means of knowledge of the truth as to the facts in question; (2) reliance, in good faith, upon the conduct or statements of the party to be estopped; and (3) action or inaction based thereon, of such a character as to change the position or status of the party claiming the estoppel, to his injury, detriment, or prejudice.[22]

The court rejected O'Connell's argument that he had a right to collect back pay from First Federal Savings and Loan and Erin Hotels as manager of the Crown Colony Entertainment Center.[23] O'Connell argued that he relied on representations made by First Federal and Erin Hotels in a management agreement.[24] The court rejected O'Connell's estoppel argument because he had the

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Entertainment Enter., 317 N.W.2d 385, 386 (N.D. 1982). His employer, Entertainment Enterprises, encountered financial difficulties and O'Connell accrued $14,988 in unpaid salary. *Id.* First Federal Savings and Loan and Erin Hotels assumed management of the Crown Colony Entertainment Center from April 16, 1980 through June 30, 1980 at which time Entertainment Enterprises resumed management. *Id.* O'Connell sued Entertainment Enterprises, First Federal, and Erin Hotels for his unpaid salary. *Id.* at 387. The court granted O'Connell summary judgment against Entertainment Enterprises for $14,988, but O'Connell was unable to execute on the judgment. *Id.* His action against First Federal and Erin Hotels was based on third-party beneficiary liability and promissory and equitable estoppel. *Id.*

20. *Id.* at 389. Section 31-11-06 of the North Dakota Century Code provides: "When a party, by his own declaration, act or omission, intentionally and deliberately has led another to believe a particular thing true and to act upon such belief, he shall not be permitted to falsify it in any litigation arising out of such declaration, act, or omission." N.D. CENT. CODE § 31-11-06 (1976).

21. 239 N.W.2d 808 (N.D. 1976).

22. *O'Connell*, 317 N.W.2d at 389 (quoting Farmers Coop. Ass'n of Churchs Ferry v. Cole, 239 N.W.2d 808, 813 (N.D. 1976)).

23. 317 N.W.2d at 387. The court granted summary judgment in O'Connell's favor on his claim for back salary against Entertainment Enterprises. *Id.*

24. *Id.* at 389. Specifically, O'Connell alleged that he relied on representations made by First Federal and Erin Hotels that all of his back salary would be paid under the new management agreements. *Id.*

means available to learn the actual facts concerning his past due salary.[25] The court found that O'Connell had access to the underlying management agreements, and that had he read the agreements he would have discovered that neither First Federal nor Erin Hotels assumed the obligation to pay his past due salary.[26]

The court's holding in *O'Connell* illustrates its reluctance to uphold an equitable estoppel claim when the plaintiff claims to be relying on a representation that is inconsistent with the written agreement between the parties, particularly when the third party seeking to estop one or both of the original parties has access to the written agreement.

Concerning the promissory estoppel claim, the court in *O'Connell* stated the elements of the rule as follows: "(1) a promise which the promissor [sic] should reasonably expect will cause the promissee [sic] to change his position; (2) a substantial change of the promissee's [sic] position through action, or forbearance; (3) justifiable reliance on the promise; and (4) injustice which can only be avoided by enforcing the promise."[27]

The court held that O'Connell failed to satisfy the elements of promissory estoppel. Specifically, O'Connell presented no evidence that he suffered a change in position by relying on the representations of First Federal and Erin Hotels.[28]

O'Connell illustrates the importance of formulating findings of fact for estoppel claims. The claimant must support every element with sufficient evidence at the trial level in order to survive appellate review. Failure to do so will lead to quick dismissals of potentially meritorious claims. Appeals are costly and time consuming; nevertheless, part of that time is well spent in assuring that all the facts necessary to support a claim are incorporated in the trial record.

The *O'Connell* decision left one question unanswered. The court recognized that a potential issue existed involving the relationship between the estoppel doctrines and the statute of frauds, but the court did not reach the merits of this issue. The court stated, "Because of our determination that O'Connell has failed to present facts which bring him within the elements of

25. *Id.* at 390.

26. *Id.* The equitable estoppel test requires that the claimant lack both knowledge and the means of obtaining knowledge. O'Connell had the means to obtain knowledge through the assumption of management. *Id.* This information clearly indicated that no one intended to pay O'Connell's back salary. *Id.*

27. *Id.* (citing Union Nat'l Bank v. Schimke, 210 N.W.2d 176, 181 (N.D. 1973)).

28. 317 N.W.2d at 390. The court stated that O'Connell's continued employment after the alleged promise to pay him back wages could not be construed to mean that he would have terminated his employment had the promise not been made. *Id.*

equitable or promissory estoppel, we find it unnecessary to address the issue of the conflict between the doctrine of estoppel and the statute of frauds."[29]

2. *Cooke v. Blood Systems, Inc.*

In *Cooke v. Blood Systems, Inc.*[30] the plaintiff attempted to make promissory estoppel a separate cause of action upon which the court could grant relief.[31] The court avoided deciding this issue, however, by deciding that the plaintiffs failed to prove the parties actually made a promise that the promisor should have reasonably expected to induce action or forbearance on the part of the promisee. The plaintiffs could not maintain a promissory estoppel claim without proof that such a promise existed between the two parties.[32]

Clearly, one of the basic elements of a promissory estoppel claim is the existence of a promise, upon which a party may reasonably rely, as opposed to mere preliminary discussions and negotiations between the parties. What will suffice to constitute such a promise, however, remains unclear.[33]

3. *Ray Co. v. Johnson*

In *Ray Co. v. Johnson*[34] the court noted that an equitable

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29. *Id.*

30. 320 N.W.2d 124 (N.D. 1982). Over a four month period Cooke and Blood Systems Inc. attempted to negotiate a lease for certain property owned by Cooke. Cooke v. Blood Sys. Inc., 320 N.W.2d 124, 126-27 (N.D. 1982). The parties never entered into a written contract. *Id.* at 127. Cooke asserted that the parties had entered into an oral contract or, at the very least, Blood Systems' actions and words constituted an oral promise upon which he had relied. *Id.* at 128-29.

31. *Id.* at 129. Cooke asked the court to adopt § 90 of the Restatement (Second) of Contracts as the basis of an estoppel claim. *Id.* Section 90(1) provides:

> A promise which the promisor should reasonably expect to induce action or forbearance on the part of the promisee or a third person and which does induce such action or forebearance is binding if injustice can be avoided only by enforcement of the promise. The remedy granted for a breach may be limited as justice requires.

RESTATEMENT (SECOND) OF CONTRACTS § 90(1) (1981).

32. 320 N.W.2d at 130.

33. *See, e.g.*, Hoffman v. Red Owl Stores, Inc., 26 Wis. 2d. 583, 133 N.W.2d 267 (1965) (promise element of promissory estoppel claim need not fulfill all the requisite elements of a formal offer: it is enough that it is an assertion that could reasonably be relied upon by the promisee).

34. 325 N.W.2d 250 (N.D. 1982). *Ray* involved a dispute over the validity of a shareholders' agreement. Ray Co. v. Johnson, 325 N.W.2d 250, 251 (N.D. 1982). The agreement included a covenant not to compete in Williams County, North Dakota, a provision allowing for the sale of certain stock in the Ray Co., and a clause rescinding the agreement upon the sale of the stock. *Id.* at 250-51.

In 1976, Robert Cook, one of the three shareholders of Ray Co., transferred 20 shares of his stock to his son pursuant to the shareholders' agreement. *Id.* Johnson, a party to the agreement, worked for Ray Co. until 1978. In 1978, he established a competing business in Divide County. *Id.* at 251. Ray Co. brought suit to enforce the covenant not to compete. *Id.* The district court found the covenant not to compete valid and enforceable. *Id.*

estoppel claim may arise even if the defendant made no express representations but, rather, simply remained silent.[35] The defendant's silence, however, standing alone is not enough; the plaintiff must also establish that the defendant had a duty to speak out and failed to do so.[36] In addition, the plaintiff must prove that she reasonably relied on the silence, and that there was a resultant change in her position.[37] In *Ray* the plaintiff failed to prove that the defendant had a duty to speak; therefore, the defendant's silence was insufficient to constitute an equitable estoppel claim.[38]

4. Hall GMC, Inc. v. Crane Carrier Co.

The court in *Hall GMC, Inc. v. Crane Carrier Co.*[39] held that when, as a part of the trial court's findings of fact regarding fraud, the lower court found that the defendant acted in good faith, did not intend to deceive the plaintiff, and did not engage in any misrepresentations, it could only reverse the trial court on equitable estoppel grounds if the trial court's findings were clearly erroneous.[40] The plaintiff also advanced a fraud claim; however, the court also similarly dismissed this claim.[41]

Hall offers another example of the importance of carefully presenting evidence and formulating findings of fact at the trial level. When a party advances two causes of action, such as fraud and equitable estoppel, the party should take great care in presenting evidence and ultimately in drafting findings of fact. Since the supreme court will only reverse a lower court when the lower court's factual conclusions are clearly erroneous, every attorney should take the time to insure the accuracy of the findings of fact and should carefully delineate those facts necessary to prove her various claims or causes of action.

5. Summary Regarding Estoppel

Regarding the estoppel doctrines, three significant issues

35. *Id.* at 254.

36. *Id.* The court held that, by the plain language of the shareholders' agreement, it was rescinded automatically upon the sale of stock. Johnson had no duty to expressly invoke the clause rescinding the agreement. *Id.*

37. *Id.* The court noted that Johnson's continued work after the parties rescinded the shareholder agreement did not prejudice the Ray Co. *Id.*

38. *Id.*

39. 332 N.W.2d 54 (N.D. 1983). The dispute in *Hall* concerned the termination of a distributorship contract. Hall GMC, Inc. v. Crane Carrier Co., 332 N.W.2d 54, 57-59 (N.D. 1983). Crane contended that Hall's action after the alleged termination of the agreement was sufficient to equitably estop it from terminating the agreement. *Id.* at 59-60. Further, Crane alleged that even if the agreement had been terminated, Hall was fraudulent in obtaining the termination. *Id.*

40. *Id.* at 60.

41. *Id.*

remain for the North Dakota Supreme Court to address: (1) whether a party may raise promissory estoppel as an independent action in North Dakota; (2) whether the court will adopt the expansive view of section 90 of the Restatement (Second) of Contracts with regards to remedies, which provides that as the courts become more willing to permit reliance as a substitute for consideration or for other elements necessary to establish a binding contract in a formalistic sense, they may adjust the remedy accordingly;[42] and (3) the extent to which a party may use the estoppel doctrines to preclude the other party from successfully asserting the statute of frauds as a defense.[43] Future cases in North Dakota will undoubtedly yield answers to these important questions.

III. INTERPRETATION ISSUES

A. GENERAL INTERPRETATION ISSUES

1. Oakes Farming Association v. Martinson Brothers

Oakes Farming Association v. Martinson Brothers[44] offers a view of several important rules that the North Dakota Supreme Court consistently follows in contract interpretation cases. First, when the court must interpret contract provisions it will read and construe the agreement in its entirety to arrive at the true intent of the parties.[45] If possible, the court's inquiry into "intent" will be

42. RESTATEMENT (SECOND) OF CONTRACTS § 90 (1979). The concluding sentence of § 90(1) provides that "[t]he remedy granted for breach may be limited as justice requires." *Id.* § 90(1).

As Professor Farnsworth noted, in conventional contract law when there is a breach:

> [T]he ineluctable consequence is that the promise itself is enforceable, and the promisee may recover the value of his expectation interest. If, however, the ground of the promisee's recovery were regarded as his reliance interest, it would seem appropriate to limit recovery to the value of that interest — the cost to the promisee of the detriment that he incurred in reliance on the promise. The Restatement Second allows the court to proceed on either course, depending on what 'justice requires' in the circumstances of that particular case.

E. FARNSWORTH, CONTRACTS § 2.19, at 96 (1982) (footnotes omitted).

This relaxation of strict contract rules regarding remedies in a breach when the breach is in the form of a reliance interest, may make the reliance interest even more appealing to the courts; but the practitioner must remember that what is won in terms of enforcement of the reliance interest may be lost or significantly limited at the remedial level.

43. *See generally* Hudec, *Restating the "Reliance Interest,"* 67 CORNELL L. REV. 704 (1982) (recent discussion of the Restatment (Second) of Contracts position on recovery based upon reliance).

44. 318 N.W.2d 897 (N.D. 1982). The *Oakes* case arose out of two sales of farm equipment and land. Oakes Farming Ass'n v. Martinson Bros., 318 N.W.2d 897, 899 (N.D. 1982). In July 1975 the Streichs sold farmland and equipment to Oakes on a contract for deed. *Id.* In December 1977 Oakes sold all of its real and tangible property to Martinson, including the property subject to the contract. *Id.* In 1978 Martinson failed to make his required payments to Oakes, who in turn was unable to pay Streich. *Id.* at 900. This lawsuit was initiated by Streich to foreclose the contract for deed. *Id.* Oakes cross-claimed against Martinson based on their sales contract. *Id.* at 900-01.

45. *Id.* at 907. Arriving at the intent of the parties from the face of the contract is at times

strictly limited to the provisions included in the writing alone.[46] If the contract is ambiguous in any respect, however, the court will examine the circumstances in which the contract was executed and the matters to which it relates.[47] The question of whether a contract is ambiguous is always a question of law.[48]

The *Oakes* decision also highlights the interrelationship between the trial court and appellate court. If the trial court determines that a contract is unambiguous, the interpretation of the contract becomes a question of law for the court to decide. In this situation, the lower court's holding need not be clearly erroneous to be reversed at the appellate level.[49] If the contract is ambiguous, however, and the trial court must refer to extrinsic evidence to interpret the agreement, those questions to which extrinsic evidence is adduced are questions for the trier of fact to determine.[50] In turn, the trial court's findings of fact can only be disturbed at the appellate level if they are clearly erroneous.[51] In *Oakes*, the interplay between these rules led the supreme court to affirm the lower court's factual determinations. The supreme court ruled that the contract in question was ambiguous as a matter of law and, therefore, the trial court's factual determinations relative to the extrinsic evidence were controlling because they could not be considered clearly erroneous.[52]

The implications of these rules are significant when drafting an agreement. The drafter should realize that if the court views the agreement as unambiguous, the court will not examine extrinsic evidence. This appears to differ slightly from the approach of the Uniform Commercial Code (Code) parol evidence rule, which applies in commercial transactions. Under the Code, even if the contract is unambiguous, the court may refer to the course of dealing, usage of the trade, and course of performance for the

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difficult. A dispute arose between Oakes and Martinson because the contract contained conflicting paragraphs. *Id.* Two paragraphs listing the property included within the contract were not consistent with one another. *Id.* Martinson alleged that he bought all the property except that specifically excluded. *Id.* Oakes alleged that Martinson only purchased the property included in paragraph 2 (c) (4) of the contract. *Id.*

46. *Id.* If the trial court answers the "intent" question from the contract alone, the court's conclusion is one of law and is fully reviewable upon appeal. *Id.*

47. *Id.* at 908. The trial court found that an ambiguity existed in the contract and used extrinsic evidence to clarify the contract. *Id.* The trial court found that the parties intended paragraph 2 (c) (4) to override paragraph I. On review the North Dakota Supreme Court found the trial court's determination was not clearly erroneous. *Id.*

48. *Id.*

49. *Id.*

50. *Id.* The court in *Oakes* noted that the determination of whether a trial court's particular finding is one of fact or law is made by the reviewing court. *Id.* Further, the reviewing court is not bound by the labels the trial court placed on the particular findings. *Id.*

51. *Id.*

52. *Id.*

purpose of explaining or supplementing the agreement's terms.[53] In addition, under the Code, if the contract does not contain a merger clause, additional consistent terms may typically be added by parol evidence.[54] The North Dakota Supreme Court appears less willing, however, as a matter of law, to permit the lower court to examine evidence to supplement or explain an agreement that is clear on its face. If the court determines that the agreement is ambiguous, however, the finder of fact may examine extrinsic evidence related to the intent issue.

2. Kelly-Springfield Tire v. Dakota Northwestern

In *Kelly-Springfield Tire v. Dakota Northwestern Bank*[55] the supreme court addressed the issue of whether and when an ambiguity is present. The court noted that an ambiguity exists whenever a good argument could be made for two contrary meanings of a given term.[56] The *Kelly* case involved a letter of credit that allowed Kelly-Springfield Tire to draw on a bank account up to $25,000 when the tire company presented a draft and commercial invoices for goods sold to Raymond Hoffman and James Mosbrucker.[57] The bank refused to honor the letter of credit

53. *See* N.D. CENT. CODE § 41-02-09 (1983) [U.C.C. § 2-202 (1978)]. Section 41-02-09 provides:

> Terms with respect to which the confirmatory memoranda of the parties agree or which are otherwise set forth in a writing intended by the parties as a final expression of their agreement with respect to such terms as are included therein may not be contradicted by evidence of any prior agreement or of a contemporaneous oral agreement but may be explained or supplemented:
>
> 1. By course of dealing or usage of trade (section 41-01-15) or by course of performance (section 41-02-15); and
> 2. By evidence of consistent additional terms unless the court finds the writing to have been intended also as a complete and exclusive statement of the terms of the agreement.

Id.

Commercial exigencies, which often make it very difficult to memorialize all the terms of an agreement in a single, tightly drafted contract, undoubtedly justify the flexible approach under the Uniform Commercial Code. This broad latitude in interpretation is not always available in noncommercial, conventional contracts. The North Dakota Century Code indicates that a written contract supercedes all oral stipulations or negotiations. *Id.* § 9-06-07 (1975). The lack of exigency, coupled with the unique nature of many noncommercial contracts may very well justify the less flexible approach regarding parol evidence in contracts outside the commercial arena. If there are strong parallels between a given noncommercial contract and a typical commercial transaction, however, a party may be able to argue that the Code should apply by analogy.

54. *See* N.D. CENT. CODE § 41-02-09 (2) (1983) [U.C.C. 2-202(b) (1978)].

55. 321 N.W.2d 516 (N.D. 1982). The dispute in *Kelly* arose out of a letter of credit issued by Northwestern Bank at the direction of Raymond Hoffman in favor of Kelly Tire. Kelly-Springfield Tire v. Dakota Northwestern Bank, 321 N.W.2d 516, 517 (N.D. 1982). Northwestern Bank issued the letter of credit so that James Mosbrucker (Hoffman's nephew and the operator of Dakota Tire) could obtain tires from Kelly Tire at better prices. *Id.*

56. *Id.* at 517-18.

57. *Id.* Northwestern Bank was to pay the letter of credit if Kelly Tire presented the bank with "(1) 'commercial invoices for goods sold to Raymond Hoffman and James Mosbrucker;' and (2) the Tire Company's written statement that it has not 'received payment from Raymond Hoffman and James Mosbrucker for a period of 30 days from the date of such invoice.'" *Id.*

refused to honor the letter of credit when the invoices referred to sales to Hoffman *or* Mosbrucker.[58] The trial court found an ambiguity, reasoning that the phrase "commercial invoices for goods sold to Raymond Hoffman and James Mosbrucker" had more than one clear meaning.[59] The supreme court disagreed and reversed the trial court as a matter of law.[60]

The court did not rest its decision entirely on its determination that an ambiguity was not present. The court stated that even if there was an ambiguity, the district court did not correctly resolve that ambiguity.[61] While the opinion appears to leave open the issue of whether extrinsic evidence may be presented to prove a latent ambiguity, it is clear that the court is very reticent to find an ambiguity when the terms of the agreement are only susceptible of one good interpretation.

3. Sorlie v. Ness

In *Sorlie v. Ness*[62] the supreme court again examined its standard rules related to the interpretation of contracts. If the contract is unambiguous and the intent of the parties can be ascertained from the writing alone, the interpretation of the contract is a question of law.[63] In determining whether a contract is ambiguous, the North Dakota Supreme Court will independently examine and construe the agreement to determine if the lower court erred as a matter of law.[64] If the court finds as a matter of law that the parties' intentions are ambiguous and that extrinsic evidence should be admitted, however, questions with regard to which extrinsic evidence is adduced are questions for the trier of fact.[65]

In *Sorlie* the court interpreted a stock transfer agreement in which Evelyn Ness agreed that in the event she desired to sell or

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58. *Id.* at 518.

59. *Id.* at 520.

60. *Id.* The court stated, "[W]hat *good* argument can be made concerning the two meanings of the phrase 'commercial invoices for goods sold to Raymond Hoffman and James Mosbrucker'? The better argument is that the phrase is clear and it means exactly what it says." (emphasis in original.) *Id.*

61. *Id.*

62. 323 N.W.2d 841 (N.D. 1982). The court in *Sorlie* interpreted a stock transfer agreement by which Evelyn Ness agreed to give Alton Glenn Sorlie an opportunity to purchase her stock in the Bismarck Tribune before she sold or transferred it to a third party. Sorlie v. Ness, 323 N.W.2d 841, 842 (N.D. 1982).

63. *Id.* at 844. Section 9-07-04 of the North Dakota Century Code provides in part that "the intention of the parties is to be ascertained from the writing alone, if possible. . . ." N.D. CENT. CODE § 9-07-04 (1975).

64. 323 N.W.2d at 844.

65. *Id.*

transfer her stock in the Bismarck Tribune Company she would grant a prior option to Alton Glenn Sorlie.[66] If Alton refused to exercise this option within 90 days, she would make a similar offer to the Bismarck Tribune Company.[67] The option agreement also expressly made the options binding upon the heirs, personal representatives, and assigns of the parties.[68]

Justice VandeWalle, writing for the majority, held that while paragraph three of the agreement dealing with the option itself seemed to refer only to sales made by Evelyn during her lifetime, paragraph four made the agreement binding on Evelyn's heirs and assigns.[69] Since the meaning and relationship of the terms in paragraph three and four were ambiguous as a matter of law, the supreme court held that the trial court properly admitted parol evidence to explain or clarify the parties' intentions with regard to the time period covered by the option.[70] The court concluded that there was an ambiguity as a matter of law because otherwise one of the provisions, paragraph three or paragraph four, would be

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66. *Id.* at 842. The stock transfer agreement provided:

> KNOW ALL MEN BY THESE PRESENTS:
> WHEREAS, STELLA IRENE MANN, of Bismarck, North Dakota, as PARTY OF THE FIRST PART, has heretofore transferred ten shares of stock in the Bismarck Tribune Company, a North Dakota corporation, Bismarck, North Dakota, to EVELYN IRENE NESS, of Whitesboro, New York, as PARTY OF THE SECOND PART, and the parties having entered into an agreement relative to the consideration thereof, DO NOW FURTHER AGREE:
> 1. That in consideration of the promises and the covenants of the parties heretofore made, the PARTY OF THE SECOND PART agrees not to assign, transfer, sell, or convey the said stock, or any part thereof, without the written consent of the PARTY OF THE FIRST PART.
> 2. That in the event it shall become necessary or should PARTY OF THE FIRST PART deem it advisable to sell all of the issued stock in the corporation to another firm or corporation, PARTY OF THE SECOND PART grants to PARTY OF THE FIRST PART full authority to assign, transfer, and convey the stock herein mentioned as fully and effectually as PARTY OF THE SECOND PART might or could do, and that payment upon such transfer shall be made to PARTY OF THE SECOND PART in accordance with a prior agreement of the parties.
> 3. That PARTY OF THE SECOND PART *specifically agrees, in the event she should desire to sell or transfer the stock, that she will grant and does grant a prior option to purchase* to Alton Glenn Sorlie at the established book value for such stock; and in the event the said Alton Glenn Sorlie shall not exercise such option to purchase within a period of ninety (90) days, then a similar offer shall be made to the Bismarck Tribune Company, and, if such company does not elect to purchase the stock, then the PARTY OF THE SECOND PART shall have the right to dispose of the same to any person as she may desire.
> 4. *That this agreement shall be binding upon the heirs, personal representatives, and assigns of the parties.*

Id. (emphasis added by the court).

67. *Id.*

68. *Id.* at 842.

69. *Id.* at 846.

70. *Id.* Whether the agreement was binding on the heirs and assigns of Evelyn Ness was the crucial determination in this case. Evelyn Ness died in 1976, and the sale in question was by her son and heir, Dale Ness. *Id.* at 843.

rendered meaningless.[71]

Having determined that there was an ambiguity as a matter of law, the court examined the oral testimony of the attorney who drafted the agreement to aid the court in ascertaining the parties' intent.[72] Based on the attorney's testimony, the court concluded that the option to Sorlie and the Bismarck Tribune Company was to take effect in the event that Evelyn Ness or her heirs tried to transfer stock outside the Ness family.[73]

Chief Justice Erickstad[74] and Justice Pederson[75] dissented. Chief Justice Erickstad construed the option agreement differently, arguing that it was intended to remain effective only during Evelyn Ness' lifetime.[76] Chief Justice Erickstad believed that nothing contained in the written agreement was susceptible to the majority's interpretation and that the court was, therefore, merely using the parol evidence rule to rewrite the agreement.[77]

Justice Pederson took a different approach. He asserted that the court should interpret the agreement strongly against the drafter, in this instance, Stella Mann.[78] He also believed the agreement was analogous to an adhesion contract, drafted by one party (Stella) and only adhered to by the other party (Evelyn).[79] As such, Justice Pederson argued the agreement should have been strictly construed to insure protection of Evelyn's interest.[80]

The *Sorlie* case illustrates the heavy burden placed on attorneys drafting agreements. By a slim majority of the court, the parties' intent, established by the testimony of Stella's attorney, prevailed. To protect one's self and one's client when drafting an agreement, the attorney should incorporate substantial written recitals of fact

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71. *Id.* at 847.
72. *Id.* at 847-48.
73. *Id.* at 848.
74. *Id.* at 849 (Erickstad, C.J., dissenting).
75. *Id.* at 850 (Pederson, J., dissenting).
76. *Id.* at 849 (Erickstad, C.J., dissenting).
77. *Id.*
78. *Id.* at 850. (Pederson, J., dissenting) Evelyn Ness acquired her stock in the Bismarck Tribune, subject to the shareholder's agreement, from Stella Mann. *Id.* at 842.

In interpreting the agreement, Justice Pederson relied on sections 9-07-14 and 9-07-19 of the North Dakota Century Code. Section 9-07-14 provides: "[I]f the terms of a promise in any respect are ambiguous or uncertain, it must be interpreted in the sense in which the promisor believed at the time of making it that the promisee understood it." N.D. CENT. CODE § 9-07-14 (1975).

Section 9-07-19 provides:

> In cases of uncertainty not removed by the preceding rules, the language of a contract should be interpreted most strongly against the party who caused the uncertainty to exist. The promisor is presumed to be such party, except in a contract between a public officer or body, as such, and a private party, and in such case it is presumed that all uncertainty was caused by the private party.

Id. § 9-07-19 (1975).
79. 323 N.W.2d at 850 (Pederson, J., dissenting).
80. *Id.*

into the agreement to assure that the intent of the parties is clear. In addition, the attorney should take great care during the drafting process to assure the express terms follow the intent elaborated in those recitals.

4. Bohn v. Bohn Implement Co.

In *Bohn v. Bohn Implement Co.*[81] an ambiguity issue was also involved. In *Bohn* the ambiguity involved a partnership agreement with a buy-out option that specified the price for buy-out to be the "capital amount" of the business.[82] An accountant testified that "capital amount" had no known definition in the accounting profession.[83] Taking this into account, the supreme court agreed with the trial court that the agreement was ambiguous on its face.[84] The court reiterated the general rule that when the court cannot ascertain the parties' intent from the writing alone, interpretation of the contract becomes a question of fact.[85]

The trial court held that the contract was ambiguous and fixed the purchase price at fair market value.[86] The supreme court affirmed the trial court's finding, holding that when an agreement concerning the price in a partnership buy-out is ambiguous, the party asserting that the agreed price is below market value must prove the validity of the agreement by clear and convincing evidence.[87] Since Graydon Bohn, the buying party, failed to meet this burden, the trial court was correct in reforming the agreement. The *Bohn* case illustrates once again the importance of clarifying the

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81. 325 N.W.2d 281 (1982).

82. Bohn v. Bohn Implement Co., 325 N.W.2d 281, 283 (1982). The partnership agreement was between Clyde and Graydon Bohn. *Id.* at 281-82. The principle business of the partnership was farming. *Id.* at 282. The buy-out provision provided:

> A. The value of the partnership interest of Clyde M. Bohn or Graydon J. Bohn, Sr., for the purpose of this agreement, shall be:
>
> a. The capital amount of the decedent's interest as shown by the books of the partnership as of the end of the last fiscal year before his death, plus
>
> b. the decedent's share of profits, or less the decedent's share of losses, of the partnership computed to the last day of the month in which his death occurred less all withdrawals prior thereto during such fiscal year. It is agreed that there is no value for goodwill or firm name and no such value has been included in the price arrived at hereinabove.

Id. at 283.

Clyde Bohn died in 1980 and Graydon Bohn informed the estate that he intended to buy out Clyde's share and offered $134,497.96. *Id.* at 282. The estate rejected the offer and this litigation ensued. *Id.*

83. *Id.* at 283. Since "capital amount" as used in the agreement was not definable, the buy-out provision was ambiguous and a buy-out amount could not be readily determined. *Id.*

84. *Id.*

85. *Id.*

86. *Id.* at 282.

87. *Id.* at 285. Section 45-09-14 of the North Dakota Century Code required the court to award the fair market value to the estate. *See* N.D. CENT. CODE § 45-09-14 (1978).

intent of the parties at the drafting stage, because absent such clarification, the court may rewrite or reform the agreement.

5. *Keller v. Hummel*

In *Keller v. Hummel*[88] the supreme court reversed the trial court's determination that the contract was not ambiguous as a matter of law.[89] Keller contracted to purchase a quonset from Hummel with final payment due on or before April 15, 1980, but Keller did not have to actually claim it until April 15, 1982.[90] Keller did not attempt to make final payment until April 1982, at which time Hummel refused to close the sale.[91] The trial court found that the sale contract was unambiguous and that the sale was completed in April 1982.[92] The supreme court reversed, finding a potential ambiguity in the time element of the contract.[93]

6. *St. Clair v. Exeter Exploration Co.*

In *St. Clair v. Exeter Exploration Co.*[94] the Court of Appeals for

88. 334 N.W.2d 200 (N.D. 1983). In *Keller* the buyer and seller of a quonset disputed the interpretation of the sales contract. Keller v. Hummel, 334 N.W.2d 200, 201-02 (N.D. 1983).

89. *Id.* at 203. The court found that the parties' intentions concerning whether time was of the essence could not be ascertained from the face of the writing alone. *Id.*

90. *Id.* at 201. While the quonset remained in Hummel's possession, Keller had a right, which he exercised, to store grain in it. *Id.*

91. *Id.* Hummel contended at trial that Keller told him that he had no use for the building and that the contract could be cancelled. *Id.*

92. *Id.* at 202 n.3. The district court awarded the quonset to Keller on a motion for partial summary judgment. *Id.* at 202. The district court left *open* for trial any claim of damage that Keller might have had against Hummel. *Id.*

93. *Id.* at 203. The supreme court was confused by the time elements in the contract. *Id.* The contract required Keller to pay for the quonset by April 15, 1980, but there were no words to indicate that failure to do so would be grounds for cancellation. *Id.* Regarding the time ambiguity, the court stated: "[U]nless the intent that time is of the essence is manifest from the face of the contract, it is a question to be determined by the trier of fact and summary judgment should not be granted if reasonable men could differ on the issue." *Id.*

The supreme court remanded the case to the trial court for trial on the issues raised by the contract. *Id.* at 204. While the supreme court did not address the contract interpretation issue, it did inform the trial court that it felt the contract should not be cancelled. *Id.* The supreme court stated in closing that "a mere dispute regarding an incidental portion of a contract which involves only the payment of money does not justify a rescission of contract." *Id.*

94. 671 F.2d 1091 (8th Cir. 1982). Clinton St. Clair and Don Bills were in the business of finding potential petroleum and gas production areas, acquiring the necessary leases to develop the areas, and selling the package to oil and gas developers for an overriding royalty. St. Clair v. Exeter Exploration Co., 671 F.2d 1091, 1092 (8th Cir. 1982). An overriding royalty is a "fractional interest in the gross production of oil and gas under a lease, in addition to the usual royalties paid to the lessor, free of any expense for exploration, drilling, development, operating, marketing, and other costs incident to the production and sale of oil and gas produced from the lease." Meeker v. Ambassador Oil Co., 308 F.2d 875, 882 (10th Cir. 1962), *rev'd*, rev'd, 375 U.S. 160 (1963).

St. Clair and Bills put together a package of leases near Bottineau and sold a one-half interest in the package to Exeter Exploration subject to a Turnkey Agreement. 671 F.2d at 1093. A Turnkey Agreement requires the developer to complete a well to the point at which it is ready for production. *Id.* at 1093 n.7 (citing Continental Oil Co. v. Jones, 177 F.2d 508 (10th Cir. 1949)). The Turnkey Agreement provided that St. Clair and Bills retained a one-eighth overriding royalty in the package. 671 F.2d at 1093. The agreement further provided that St. Clair would be entitled to a one-sixteenth

the Eighth Circuit held that in determining whether there is an ambiguity in the terms of an agreement, the court should examine the disputed language in the context of the entire agreement.[95] The court added that evidence relating to prior negotiations and other circumstances surrounding the making of the contract should be considered in determining whether the contract is in fact ambiguous.[96]

The court of appeals applied the parol evidence rule in *St. Clair* with a laxity that may not be characteristic of the North Dakota Supreme Court's analysis. The eighth circuit, applying North Dakota law, was willing to look at extrinsic evidence to determine whether or not there was a latent ambiguity.[97] The Supreme Court of North Dakota, however, appears to limit its analysis much more circumspectly to the four corners of the agreement when interpreting a contract not covered by the Uniform Commercial Code.[98] This apparent difference, at least as a matter of degree, in terms of how the Court of Appeals for the Eighth Circuit and the North Dakota Supreme Court view extrinsic evidence to determine whether or not an agreement is ambiguous, may make it worthwhile for an attorney with a parol evidence problem to do some forum shopping, whenever possible.

B. SPECIFIC INTERPRETATION ISSUES: COVENANTS NOT TO COMPETE

1. Ray Co. v. Johnson

The supreme court in *Ray Co. v. Johnson*[99] used two rules of interpretation in construing a covenant not to compete. First, the

overriding royalty in any additional property added to the package. *Id.*

The initial drilling in the package area was unsuccessful. *Id.* at 1094. St. Clair and Bills renegotiated some leases within the package and entered into a Letter Agreement that concerned drilling the specific leases. *Id.* The Letter Agreement had a twelve month expiration date. *Id.* The drilling was once again unsuccessful. *Id.*

Finally, Exeter Exploration entered into a separate lease agreement to drill on land that was included in both the original Turnkey Agreement and the Letter Agreement. *Id.* The drilling resulted in producing wells and St. Clair demanded payment of his overriding royalty pursuant to the Turnkey Agreement. *Id.* at 1095. Exeter refused to pay, alleging that the Letter Agreement, which had expired, controlled payment of the royalties in question. *Id.*

The federal district court noted that the existence of the two agreements created an ambiguity concerning which agreement was controlling. *Id.* The court, therefore, admitted parol evidence. Based on the parol evidence, the court found the Turnkey Agreement controlling. *Id.*

95. 671 F.2d at 1095-96.

96. *Id.* at 1096.

97. *Id.*

98. *See* Oakes Farming Ass'n v. Martinson Bros., 318 N.W.2d 897 (N.D. 1982) (the North Dakota Supreme Court effectively limited its analysis of a potential ambiguity to the four corners of the document). See *supra* notes 44-54 and accompanying text for a discussion of *Oakes*.

99. 325 N.W.2d 250 (N.D. 1982). See *supra* note 34 for a discussion of the facts in *Ray Co. v. Johnson*.

court reasoned that because it had determined that the ambiguity in the agreement could be resolved by examining the written agreement alone, the parol evidence offered by the plaintiff was inadmissible.[100] Second, the court noted that an ambiguity would be construed against the drafter of the agreement who supposedly protected his or her best interests in drafting the agreement.[101] Using these two rules of construction, the supreme court reversed the trial court and held that since the agreement had terminated by its own terms, it was not necessary to determine the scope or enforceability of the covenant not to compete.[102]

2. Hawkins Chemical, Inc. v. McNea

In *Hawkins Chemical, Inc. v. McNea*[103] Hawkins and McNea entered into an agreement, which included a covenant not to compete in a six state area, including North Dakota.[104] Under the North Dakota Century Code, a covenant not to compete is only enforceable if the geographic area is within a specified county, city, or a part of either.[105] The trial court ruled that the covenant Hawkins and McNea entered into was overbroad, and therefore was void.[106] The supreme court, however, reformed the agreement to make the covenant not to compete enforceable in Ward County.[107] The court believed the contract should be reformed

100. Ray Co. v. Johnson, 325 N.W.2d 250, 251-52 (N.D. 1982) (citing Sorlie v. Ness, 323 N.W.2d 841, 844 (N.D. 1982)). See *supra* notes 62-80 and accompanying text for a discussion of *Sorlie v. Ness*.

101. 325 N.W.2d at 252 (citation omitted). *See also* N.D. CENT. CODE § 9-07-19 (1975). Section 9-07-19 provides in part that "[i]n cases of uncertainty. . . the language of the contract should be interpreted most strongly against the person who caused the uncertainty to exist." *Id.*

102. 325 N.W.2d at 253.

103. 321 N.W.2d 918 (N.D. 1982). Hawkins Chemical purchased Mon-Dak Corporation from Lloyd McNea and R. F. Saunders. Hawkins Chemical, Inc. v. McNea, 321 N.W.2d 918, 918-19 (1982). As part of the total agreement McNea and Saunders entered into a covenant not to compete with Mon-Dak in a six state area, which included North Dakota. *Id.* at 919. Hawkins paid $218,000 for the noncompetition agreement, which was separate from the sales contract. *Id.* Shortly thereafter, McNea began a chemical sales business in Ward County, North Dakota in violation of the agreement. *Id.* Hawkins Chemical brought suit to enjoin McNae from further operation of his business. *Id.*

104. *Id.*

105. N.D. CENT. CODE § 9-08-06(1) (1975). Section 9-08-06(1) provides:

> Every contract by which anyone is restrained from exercising a lawful profession, trade, or business of any kind is to the extent void, except:
>
> 1. One who sells the good will of a business may agree with the buyer to refrain from carrying on a similar business within a specified county, city or a part of either, so long as the buyer or any person deriving title to the good will from him carries on a like business therein.

Id.

106. 321 N.W.2d at 919.

107. *Id.* at 920. The court noted that it had previously reformed covenants not to compete to conform with § 9-08-06. *Id.* at 919-20.

For example of a case in which the court reformed an overboard covenant not to compete, see

since the seller had presumably received pecuniary compensation for the covenant and, therefore, should not be allowed to escape entirely from the consequences of his promise.[108]

Justice VandeWalle dissented because he would not have reformed the agreement.[109] He added that since the court reformed the agreement, he believed the covenant should be enforced in the county where the business was presently located rather than in Ward County.[110]

Any attorney that drafts a covenant not to compete in an agreement for the sale of a business should pay specific attention to the limitations placed on these covenants in North Dakota Century Code section 9-08-06.[111] Although the court in *Hawkins* reformed the overbroad covenant, the disagreement between the majority and Justice VandeWalle over the area covered by the reformed covenant illustrates the importance of having the parties determine the covenant's coverage rather than leaving the issue to the courts.

C. SPECIFIC INTERPRETATION ISSUES: QUASI-CONTRACTS

1. Jerry Harmon Motors, Inc. v. Heth

In *Jerry Harmon Motors, Inc. v. Heth*[112] a dispute arose over the payment for a conversion kit installed in a new van Gary Heth purchased from Jerry Harmon Motors.[113] The auto dealer claimed that the parties had reached a binding agreement whereby the defendant agreed to pay for the conversion kit as an additional charge.[114] Heth claimed that the cost of the conversion kit was included in the cost of the vehicle.[115] The trial court held that all of

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Igoe v. Atlas Ready-Mix, Inc., 134 N.W.2d 511 (N.D. 1965) (court struck Mandan from a covenant not to compete in Bismarck and Mandan, North Dakota).

108. 321 N.W.2d at 919. Hawkins Chemical contracted to pay an additional $218,000 for the covenant not to compete over a period of three years. *Id.* Hawkins had already paid $150,000. *Id.*

109. *Id.* at 920-21 (VandeWalle, J., concurring in part and dissenting in part).

110. *Id.* at 921 (VandeWalle, J., concurring in part and dissenting in part). Hawkins Chemical was running a business in McLean County rather than Ward County. *Id.* Justice VandeWalle indicated, therefore, that the covenant not to compete should have been for McLean County. *Id.*

111. N.D. CENT. CODE § 9-08-06 (1975). See *supra* note 105 for the pertinent portion of § 9-09-06.

112. 316 N.W.2d 324 (N.D. 1982).

113. Jerry Harmon Motors, Inc. v. Heth, 316 N.W.2d 324. 325 (N.D. 1982). The conversion kit changed the van from two-wheel to four-wheel drive. *Id.* Heth and Harmon Motors entered into a retail installment contract in which Heth was to pay $8800 for a 1975 GMC four-wheel drive van. *Id.* Heth paid the down payment of $1800 and left the dealership to obtain insurance. *Id.* Upon his return, Harmon Motors informed him that the price of the vehicle did not include the conversion kit. *Id.* The dispute arose over who would bear the cost of the conversion kit. *Id.*

114. *Id.*

115. *Id.* Apparently, a considerable discussion took place between Heth and Harmon Motor's credit manager, Jess Ditworth, over who would bear the cost of the conversion kit. *Id.* At the conclusion of the discussion each party believed the other was going to pay for the conversion kit and that the kit would cost no more than $2000. *Id.*

the formalities necessary to constitute an enforceable contract concerning the conversion kit were not present, but held in favor of Jerry Harmon Motors based on quasi-contract.[116] The Supreme Court of North Dakota affirmed.[117] The court noted that recovery on quasi-contract was based on the theory of unjust enrichment.[118] In *Harmon* the court found that the benefit was the kit, which Heth had retained but in equity belonged to the dealer.[119]

In calculating the damages based on unjust enrichment or quasi-contract, the supreme court noted that the trial court had failed to make a finding concerning the understanding between the parties regarding the cost of the kit.[120] Although an issue of fact would normally be remanded to the lower court as the trier of fact, the supreme court decided that it should make indispensable findings of fact in order to promote justice and judicial economy.[121] The court examined the evidence and concluded that the defendant understood that he would have to pay for the cost of the conversion kit in an amount not to exceed $2000.[122] The supreme court, therefore, reduced the trial court's $3168 damage award to $2000.[123]

IV. SPECIFIC INTERPRETATION ISSUES

A. TIME IS OF THE ESSENCE CLAUSES

1. Keller v. Hummel

In *Keller v. Hummel*[124] the contract's status rested on whether there was an enforceable time is of the essence clause.[125] If there was an enforceable time is of the essence clause, Keller's failure to tender payment at the specified time discharged Hummel from any further obligation.[126] If time was not of the essence, however,

116. *Id.* at 327.

117. *Id.* at 330.

118. *Id.* at 328. *See Contract, Tort and Restitution — A Satisfactory Division or Not?*, 99 LAW Q. REV. 217, 233-34 (1983). The author asserts that the courts should drop the facade of implied or quasi-contract and admit that their opinions are based on a desire to avoid unjust enrichment of a party. *Id.*

119. 316 N.W.2d at 330.

120. *Id.* at 329. The trial court did find, however, that Gary Heth was liable for the cost of the conversion kit. *Id.*

121. *Id.* at 330.

122. *Id.* The credit manager of Jerry Harmon Motors testified that he told Heth that the cost of the conversion kit would be between $1200 and $2000. *Id.* at 325.

123. *Id.* at 330. The supreme court apparently believed that Heth could not impliedly agree to pay more for the conversion kit than the top price quoted by the auto dealer at the time of the sale. *Id.*

124. 334 N.W.2d 200 (N.D. 1983). See *supra* notes 88-93 and accompanying text for a discussion of the facts in *Keller v. Hummel.*

125. Keller v. Hummel, 334 N.W.2d 200, 203 (N.D. 1983). The sales agreement stated that Keller was to make a down payment of $2000 by April 25, 1979 and pay the remaining $1500 by April 15, 1980. *Id.* at 201. The agreement did not state what should happen if payment was late. *Id.*

126. *Id.* at 203.

Keller could tender payment within a reasonable time.[127] The North Dakota Supreme Court held, however, that it could not determine whether time was of the essence from the writing alone and remanded the case to permit the parties to present extrinsic evidence to determine the issue.[128]

2. *E.E.E., Inc. v. Hanson*

In *E.E.E., Inc. v. Hanson*[129] the North Dakota Supreme Court reiterated the general rule that when time, either expressly by the terms of the contract or by a reading of the intent of the parties, is of the essence, the parties must perform at the exact time specified in the contract.[130]

If a time is of the essence clause is included in a contract, the parties must perform within the specified time.[131] Even if the clause is not expressly provided, the court may rule that the intentions of the parties were sufficient to make time of the essence.[132] An attorney should take special care in advising clients concerning time is of the essence clauses because the failure to perform at the specified time releases the other party of all future obligations under the agreement. Under any circumstances, the attorney must apprise a client of the necessity of performing on time if such a clause is included or intended in a contract, and the attorney should discuss the matter with the client at the drafting stage.

B. ACCELERATION CLAUSES

1. *Johnson v. King*

The defendant, King, in *Johnson v. King*[133] executed three

127. *Id.* at 203-04. The court noted that the determination of whether the payment is tendered within a "reasonable time" is a fact question that must be decided on a case by case basis. *Id.* at 203.

128. *Id.* at 204. The case was before the supreme court on appeal after the trial court had granted a motion for summary judgment. *Id.* The court did not have a sufficient record, therefore, to reach the merits. *Id.*

129. 318 N.W.2d 101 (N.D. 1982). See *supra* notes 6-12 and accompanying text for a discussion of the facts in *E.E.E., Inc. v. Hanson.*

130. E.E.E., Inc. v. Hanson, 318 N.W.2d 101, 104 (N.D. 1982). *See* N.D. CENT. CODE § 9-07-23 (1975). Section 9-07-23 provides that "[t]ime is of the essence of a contract if it is provided expressly by the terms of the contract or if such was the intention of the parties as disclosed thereby." *Id.*

131. 318 N.W.2d at 104. *See also* Fargusson v. Talcott, 7 N.D. 183, 186-87, 73 N.W. 207, 208 (1897). Referring to a contract with a "time is of the essence" clause, the North Dakota Supreme Court in *Fargusson* stated that "in such a case failure to comply with the terms of the contract, at the time named therein for performance, will debar the person in default from claiming any rights thereunder, even in a court of equity." *Id.* at 188, 73 N.W. at 208.

132. 318 N.W.2d at 104. *See* N.D. CENT. CODE § 9-07-23 (1975). See *supra* note 130 for the text of § 9-07-23.

133. 325 N.W.2d 254 (N.D. 1982).

documents: a $500,000 promissory note payable to the plaintiff, Johnson, on April 1, 1985; a mortgage deed on certain described property securing the note; and an assignment of rents on the property covered by the deed.[134] The note provided for biannual payments of interest until April 1, 1985, when the balance of the note was due.[135] The promissory note did not include an acceleration clause, but the mortgage did.[136] King, the defendant, failed to make an interest payment when due, and the Johnsons attempted to foreclose on the property.[137]

The court noted that the general rule with regard to acceleration clauses was that an acceleration clause in a note accelerated a mortgage, even if the mortgage did not contain an acceleration provision.[138] The court further noted that most jurisdictions hold that even when there is no acceleration clause in the note, an acceleration clause in the mortgage will enable the holder to accelerate the maturity if there is a breach.[139] The court, however, continued to follow what it perceived to be the minority rule that the acceleration clause in a mortgage is not transferred to and does not become a part of a promissory note unless the agreement specifically so provides.[140]

This position treats the note and mortgage as separate and distinct instruments.[141] In the event of default, the mortgagee has an election of remedies. She may sue on the note and obtain a personal judgment, or she may proceed against the security of the mortgage and apply the proceeds of the foreclosure sale to the debt.[142] The mortgagee, however, may not obtain double satisfaction or relief.[143] The court, therefore, reasoned that an acceleration clause in a mortgage would not become a part of a promissory note unless the contracting parties specifically so provided.[144] As *King* amply illustrates, the drafter should be

134. Johnson v. King, 325 N.W.2d 254, 255 (N.D. 1982).

135. *Id.*

136. *Id.* at 255-56. The acceleration clause stated that "if default be made by the party of the first part in any of the foregoing provisions it shall be lawful for the parties of the second part, their heirs, executors, administrators, successors or assigns, or their attorney to declare the whole sum above specified to be due." *Id.*

137. *Id.* at 256. The Johnsons appealed the denial of their motion for summary judgment. *Id.*

138. *Id.* (citing 55 AM. JUR. 2D *Mortgages* § 379, at 476-77 (1971)).

139. 325 N.W.2d at 256.

140. *Id.* at 256-57. The court referred to the language in American Jurisprudence Second that stated "there is also authority proceeding upon the theory that an acceleration provision in a mortgage securing a note does not affect the maturity of the note for purposes other than that of foreclosure of the mortgage." 55 AM. JUR. 2D *Mortgages* § 379, at 426-27 (1971).

141. *See* Winne v. Lahart, 155 Minn. 307, 193 N.W. 587, 588 (1923) (a note and a mortgage are separate instruments and the negotiable character of the note does not affect the character of the mortgage).

142. 325 N.W.2d at 257.

143. *Id.*

144. *Id.*

careful to include acceleration clauses in both the promissory note and the mortgage to insure that the mortgagee's remedies are not limited in the event of default.

V. DEFENSES TO FORMATION OR ENFORCEMENT

A. FRAUD

1. Pioneer Credit Co. v. Medalen

The court in *Pioneer Credit Co. v. Medalen*[145] stated that failure to read the contract would not excuse the party from her obligations.[146] The court did, however, note an exception to this rule when the party can establish that she was prevented from reading the document by fraud, artifice, or design by the other party.[147]

2. Hall GMC, Inc. v. Crane Carrier Co.

The court in *Hall GMC, Inc. v. Crane Carrier Co.*[148] examined a series of issues related to the termination of a distributorship agreement.[149] The manufacturer, Crane, claimed that the distributor, Hall, acted fraudulently when Hall exchanged three refuse trucks for four concrete mixers and requested correction on the Manufacturer's Statement of Origin to reflect that the mixers were 1980 models.[150] The changes insured that Hall would receive 100% of the net cost for the 1980 models when he terminated the distributorship.[151] Crane argued that Hall's actions were intended to deceive and mislead him into believing that Hall would continue to be a distributor, when in fact the exchange was merely to recoup 100% of the net cost upon termination.[152]

145. 326 N.W.2d 717 (N.D. 1982). See *supra* notes 13-18 and accompanying text for a discussion of the facts in *Pioneer Credit Co. v. Medalen*.

146. Pioneer Credit Co. v. Medalen, 326 N.W.2d 717, 719 (1982).

147. *Id.* The affidavits presented to the trial court indicated that Medalen's failure to read the "Guarantee of Payment" was entirely his own fault. *Id.* As a result, the court applied the general rule that failure to read a contract does not excuse performance. *Id.*

148. 332 N.W.2d 54 (N.D. 1982). Previously, this Article discussed *Hall* with regard to the issue of equitable estoppel. See *supra* notes 39-43 and accompanying text for the discussion of *Hall GMC, Inc. v. Crane Carrier Co.*

149. Hall GMC, Inc. v. Crane Carrier Co., 332 N.W.2d 54, 57 (N.D. 1982).

150. *Id.* at 59-60. Hall testified at trial that he had the manufacturer's statement of origin changed to indicate that the four concrete mixers were 1980 models to facilitate their sale and to improve the possibility that Crane would repurchase them if they terminated the distributorship agreement. *Id.* at 58.

151. *Id.* at 59. *See* N.D. CENT. CODE § 51-07-01 (1982) (upon termination of a distributorship agreement, the manufacturer must buy back all current year vehicles held by the retailer at 100% of net cost).

152. 332 N.W.2d at 59-60.

The court recognized that the case presented the potential of both actual and constructive fraud as defined in the North Dakota Century Code.[153] The court held, however, that Crane had not proven the claims based on fraud.[154] The court concluded that the trial court's determinations that Hall's decision to terminate was in good faith, that he did not intend to deceive Crane, and that he had not made any misrepresentations were not clearly erroneous.[155]

The court emphasized that under North Dakota law Crane was charged with knowledge of the laws of the state, including the statutory right of termination in distributorship agreements.[156] The court, therefore, did not accept Crane's argument that he was misled by Hall, because he was charged with the knowledge that amending the manufacturer's statement of origin would not limit Hall's statutory right to terminate the distributorship agreement.[157]

B. STATUTE OF FRAUDS

1. Hofmann v. Stoller

In *Hofmann v. Stoller*[158] the parties entered into an oral

153. *Id.* Fraud in North Dakota is defined as either actual or constructive. N.D. CENT. CODE § 9-03-07 (1975). Actual fraud is defined at N.D. CENT. CODE § 9-03-08 (1975). Section 9-03-08 provides:

> Actual fraud within the meaning of this title consists in any of the following acts committed by a party to the contract, or with his connivance, with intent to deceive another party thereto or induce him to enter into the contract:
> 1. The suggestion as a fact of that which is not true by one who does not believe it to be true;
> 2. The positive assertion, in a manner not warranted by the information of the person making it, of that which is not true though he believes it to be true;
> 3. The suppression of that which is true by one having knowledge or belief of the fact;
> 4. A promise made without any intention of performing it; or
> 5. Any other act fitted to deceive.

Id. Constructive fraud is defined at N.D. CENT. CODE § 9-03-09 (1975). Section 9-03-09 provides:

> Constructive fraud consists:
> 1. In any breach of duty which, without an actually fraudulent intent, gains an advantage to the person in fault or anyone claiming under him, by misleading another to his prejudice or to the prejudice of anyone claiming under him; or
> 2. In any such act or omission as the law specially declares to be fraudulent without respect to actual fraud.

Id.

154. 332 N.W.2d at 60. The court did note that Hall's conduct in terminating the distributorship agreement bordered on fraud. *Id.*

155. *Id.* The supreme court issued its usual reminder that when the evidence is conflicting, it will normally defer to the trial court's determination of fact since it had the opportunity to weigh and assess the credibility of the witnesses. *Id.*

156. *Id.*

157. *Id.*

158. 320 N.W.2d 786 (N.D. 1982).

agreement whereby Stoller leased a farmstead and milking barn for one year from Hofmann.[159] Two months into the lease a fire destroyed the milking barn and Stoller and Hofmann entered into a second oral agreement whereby Stoller was allowed to share Hofmann's barn until his barn was rebuilt.[160] A dispute arose over what Stoller was to pay under the second oral agreement and Stoller asserted the statute of frauds as a defense.[161] After losing at the trial court level, Stoller appealed asserting that the trial court applied an improper standard of proof in determining whether the agreement was partially performed and thus exempt from the statute of frauds.[162] Stoller argued that for purposes of the statute of frauds the court must find that the contract was partially performed by clear and convincing evidence.[163] The North Dakota Supreme Court, however, agreed with the trial court and concluded that the Uniform Commercial Code applied in this case and that it had the effect of relaxing the standard of proof for excepting agreements from the statute of frauds.[164] The court, therefore, applied the Uniform Commercial Code standard of a preponderance of the evidence rather than the clear and convincing standard that the

159. Hofmann v. Stoller, 320 N.W.2d 786, 788 (N.D. 1982). There was no dispute over the terms of the first lease agreement. *Id.*

160. *Id.*

161. *Id.* Stoller's cows were fed grain and minerals from Hofmann's supply. *Id.* His cows also grazed on Hofmann's land. *Id.* The dispute in this case was over the amount Stoller was to pay for feed, grain, minerals, grazing rights, and electricity. *Id.* Stoller insisted that he was to pay nothing. *Id.* Hofmann insisted that he was to pay one-half of the total cost for the entire operation. *Id.*

162. *Id.* at 790. The trial court held that the feed and minerals contract was controlled by the Uniform Commercial Code, specifically § 41-02-08 of the North Dakota Century Code and the exception to the statute of frauds found at § 41-02-08 (3) (c). *Id.* Section 41-02-08 provides in part:

> 1. Except as otherwise provided in this section a contract for the sale of goods for the price of five hundred dollars or more is not enforceable by way of action or defense unless there is some writing sufficient to indicate that a contract for sale has been made between the parties and signed by the party against whom enforcement is sought or by his authorized agent or broker. A writing is not insufficient because it omits or incorrectly states a term agreed upon but the contract is not enforceable under this paragraph beyond the quantity of goods shown in such writing. . . .
> . . . .
> 3. A contract which does not satisfy the requirements of subsection 1 but which is valid in other respects is enforceable. . . .
> c. With respect to goods for which payment has been made and accepted or which have been received and accepted (section 41-02-69).

N.D. CENT. CODE § 41-02-08 (1983).

The trial court found by a preponderance of the evidence that Stoller received and accepted grain and minerals for his cows and therefore the statute of frauds was not a bar to Hofmann's recovery on the oral contract. 320 N.W.2d at 791.

163. 320 N.W.2d at 790. Stoller based his argument on Buettner v. Nostdahl, 204 N.W.2d 187 (N.D. 1973). *Buettner* requires that before a contract may be excepted from the statute of frauds, the existence of the contract must be shown by clear and convincing evidence and the acts relied upon as constituting part performance must unmistakenly point to the existence of the agreement. 204 N.W.2d at 195.

164. 320 N.W.2d at 790. The supreme court distinguished *Buettner* on the grounds that it was a non-Code transaction and was not applicable. *Id.*

court has applied in noncommercial contract cases in North Dakota.[165]

C. AGENCY

1. Cook v. Jacklitch & Sons, Inc.

In *Cook v. Jacklitch & Sons, Inc.*[166] the defendant claimed that he was not personally liable under a contract because he was acting solely as an agent for a corporation.[167] The court reviewed the record and refused to limit the defendant's personal liability.[168] The court stressed that the plaintiffs believed they were contracting with the defendant in his individual capacity, that there was no discussion between the parties regarding the defendant's agency status, and that the defendant's signature did not indicate that he was signing only in a representative capacity.[169]

VI. REMEDIAL ISSUES

A. DAMAGES

1. Hirschkorn v. Severson

The trial court in *Hirschkorn v. Severson*[170] dismissed the plaintiff's action and held for the defendant on his counterclaim.[171] The trial court awarded interest to the defendant at the rate of ten percent even though there was no interest rate expressed in any written agreement between the parties.[172] The trial court

165. *Id.*

166. 315 N.W.2d 660 (N.D. 1982). The Cooks entered into a written contract to have Jacklitch & Sons build them a house. Cook v. Jacklitch & Sons, Inc., 315 N.W.2d 660, 661 (N.D. 1982). After construction began, the Cooks ordered Jacklitch & Sons to stop working because they were performing negligently. *Id.* The trial court found that the Cooks were justified in terminating the contract and awarded the Cooks $2500 in compensatory damages. *Id.* The trial court also found Leroy Jacklitch personally liable on the contract. *Id.* at 664.

167. *Id.*

168. *Id.*

169. *Id.*

170. 319 N.W.2d 475 (N.D. 1982). *Hirschkorn* involved an action by the plaintiffs to establish the existence of an oral contract to buy out the defendant's interest in a small corporation. Hirschkorn v. Severson, 319 N.W.2d 475, 476 (N.D. 1982). The defendant counterclaimed for past due dividends. *Id.*

171. *Id.* at 479-80. The trial court found that the plaintiffs breached their fiduciary duty to the defendant in not paying him dividends. *Id.*

172. *Id.* at 480. In awarding the 10% interest rate the trial court apparently did not apply § 47-14-05 of the North Dakota Century Code. Section 47-14-05 provides:

> *Interest for any legal indebtedness shall be at the rate of six percent per annum unless a different rate not to exceed the rate specified in section 47-14-09 is contracted for in writing.* All contracts shall bear the same rate of interest after maturity as they bear before maturity, and any

acknowledged the defendant's argument that *Klitzke v. Klitzke*,[173] a divorce case, constituted persuasive precedent for awarding interest above the legal rate on equitable grounds.[174]

However, the supreme court reversed the trial court on the interest issue noting that if it allowed the lower court's holding to stand, the variation of interest rates awarded in actions would arbitrarily be based on whether the case was legal or equitable.[175] The court believed such a distinction was unfair and would be difficult to ascertain.[176] Although the court admitted that awarding only the legal rate of interest, six percent, was inequitable, it felt constrained by section 47-14-05 of the North Dakota Century Code to limit prejudgment interest to six percent.[177]

The *Hirschkorn* case emphasizes the importance of providing an interest rate clause in most contracts to insure that judgments based on the breach of the agreement are subject to interest at a rate nearer the market rate. Without such a provision, it is likely that there may be instances when the prolonging of a law suit in a major case may be economically worthwhile to one of the parties, because the legal rate of interest is much less than prevailing market rates. A party might, therefore, deem it worthwhile to avoid payment of its contractual obligations for a lengthy period of time, particularly in cases that present legitimate legal issues, to take advantage of the abnormally low legal rate payable on such judgments. In cases involving substantial sums of money, the legal rate of six percent may constitute a disincentive to settlement in marginal cases and may actually serve as an incentive to prolong lawsuits. Evidently, with these arguments in mind, Justice VandeWalle appeared to have been endeavoring to send a message to the legislature, encouraging it to consider a flexible rate of prejudgment interest as

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> contract attempting to make the rate of interest higher after maturity shall be void as to such increase of interest, except for a charge for late payment penalty charged in addition to interest which may not exceed fifteen dollars or fifteen percent of the late payment, whichever is less, unless otherwise agreed to in the real estate note or mortgage.

N.D. CENT. CODE § 47-14-05 (Supp. 1983) (emphasis added). The court, therefore, remanded with instruction to apply the legal rate of six percent per annum. 319 N.W.2d at 480.

173. 308 N.W.2d 385 (N.D. 1981).

174. 319 N.W.2d at 480. In *Klitzke* the supreme court stated that § 47-14-05 did not limit a court's ability to make an equitable distribution of property in a divorce and that in doing so, the court could require a party to pay interest at a higher rate than the statutory rate. Klitzke v. Klitzke, 308 N.W.2d 385, 390 (N.D. 1981).

175. 319 N.W.2d at 480. The court distinguished *Klitzke* stating that since it was a divorce action, the award of interest was controlled by § 14-05-24. *Id. See* N.D. CENT. CODE § 14-05-24 (1981) (grants the court broad powers to make equitable distributions of property in divorce cases).

176. 319 N.W.2d at 480.

177. *Id.*

a statutory matter.[178] Legislative activity in this area would appear to be particularly appropriate.

2. Hofmann v. Stoller

The court in *Hofmann v. Stoller*[179] noted the difference between incidental damages, which are recoverable by a seller, and consequential damages, which are not recoverable.[180] The court stated:

> While the distinction between the two is not an obvious one, the [Uniform Commercial] Code makes plain that incidental damages are normally incurred when a buyer (or seller) repudiates the contract or wrongfully rejects the goods, causing the other to incur such expenses as transporting, storing, or reselling the goods. On the other hand, consequential damages do not arise within the scope of the immediate buyer-seller transaction, but rather stem from losses incurred by the non-breaching party in its dealings, often with third parties, which were a proximate result of the breach, and which were reasonably foreseeable by the breaching party at the time of contracting.[181]

The distinction between consequential and incidental damages set forth in *Hofmann* remains unclear. The language, however, does appear to lay out certain guidelines within which to marshall one's evidence on such damage issues.[182]

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178. *Id.* In the opinion of the court, Justice VandeWalle noted that the six percent rate was inequitable, but he indicated that flexible interest rates could only be established by statute. *Id.*

179. 320 N.W.2d 786 (N.D. 1982). See *supra* notes 158-64 and accompanying text for a discussion of the factual situation underlying *Hofmann v. Stoller.*

180. Hofmann v. Stoller, 320 N.W.2d 786, 792 (N.D. 1982).

181. *Id.* (quoting Petroleo Brasileiro, S.A., Petro v. Ameropan Oil Corp., 372 F.Supp. 503, 508 (E.D.N.Y. 1974)).

182. Further help in this area may be found in the Uniform Commercial Code as codified in the North Dakota Century Code. *See* N.D. CENT. CODE tit. 41 (1983).

It is important to note that the Century Code limits a seller to incidental damages. N.D. CENT. CODE § 41-02-89 (1983). Section 41-02-89 [U.C.C. § 2-710 (1978)] provides: "Incidental damages to an aggrieved seller include any commercially reasonable charges, expenses, or commissions incurred in stopping delivery, in the transportation, care, and custody of goods after the buyer's breach, in connection with return or resale of the goods, or otherwise resulting from the breach." *Id.*

An aggrieved buyer, however, is entitled to both incidental damages and consequential damages. *Id.* § 42-02-94. Section 41-02-94 [U.C.C. § 2-715 (1978)] provides:

> 1. Incidental damages resulting from the seller's breach include expenses reasonably incurred in inspection, receipt, transportation, and care and custody of goods rightfully rejected, any commercially reasonable charges, expenses, or commissions in connection with effecting cover, and any other reasonable expense incident to the delay or other breach.

3. Kulseth v. Rotenberger

The court in *Kulseth v. Rotenberger*[183] allowed a contractor to recover under *quantum meruit*, although he did not substantially perform his obligations under the contract.[184] The court noted that to recover under *quantum meruit* the contractor must prove the value of his performance before the owner has the burden to prove a lack of substantial performance and the reduction in value or cost of repairs attributable to the contractor's breach.[185] The court acknowledged the definition of *quantum meruit* as provided in section 374 of the Restatement (Second) of Contracts.[186]

4. Storebo v. Foss

In *Storebo v. Foss*[187] the court noted that the proper measure of damage when a contractor breaches a construction contract, which cannot be remedied without reconstruction or material injury to a substantial portion of the building, is diminution in value.[188] The court, however, affirmed the lower court's holding that awarded

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2. Consequential damages resulting from the seller's breach include:
   a. Any loss resulting from general or particular requirements and needs of which the seller at the time of contracting had reason to know and which could not reasonably be prevented by cover or otherwise; and
   b. Injury to person or property proximately resulting from any breach of warranty.

Id.

183. 320 N.W.2d 920 (N.D. 1982). Russell Kulseth was a builder who contracted to build a shop for Bill Rotenberger. Kulseth v. Rotenberger, 320 N.W.2d 920, 921 (N.D. 1982). When the building was close to completion, a dispute arose and all work stopped. *Id.* Rotenberger refused to pay the full contract price and Kulseth sued to recover in *quantum meruit*. *Id.* at 922.

184. *Id.* at 923. Testimony at trial indicated that the shop was 90% completed. *Id.* at 921.

185. *Id.* at 923.

186. *Id.* Section 374 of the Restatement (Second) of Contracts provides:

> (1) Subject to the rule stated in Subsection (2), if a party justifiably refuses to perform on the ground that his remaining duties of performance have been discharged by the other party's breach, the party in breach is entitled to restitution for any benefit that he has conferred by way of part performance or reliance in excess of the loss that he has caused by his own breach.
>
> (2) To the extent that, under the manifested assent of the parties, a party's performance is to be retained in the case of breach, that party is not entitled to restitution if the value of the performance as liquidated damages is reasonable in the light of the anticipated or actual loss caused by the breach and the difficulties of proof of loss.

RESTATEMENT (SECOND) OF CONTRACTS § 374 (1981).

187. 325 N.W.2d 223 (N.D. 1982). This case arose when Gerald Foss refused to pay for cement work done by Donald Storebo, claiming that the work did not conform to the contract. Storebo v. Foss, 325 N.W.2d 223, 224 (N.D. 1982). Storebo filed a mechanics' lien against the property in question and Foss counterclaimed for damages. *Id.*

188. *Id.* at 225. In *Storebo*, the court could have determined diminution of value damages by subtracting the value of the property with the defective basement from the value of the property with a properly constructed basement. *Id.*

damages based on the expense that Foss would incur to make the work conform to the agreement.[189] The supreme court concluded that "the trial court could properly find that the defects in the basement floor could be remedied without taking down and reconstructing a substantial portion of the building."[190]

5. Hall GMC, Inc. v. Crane Carrier Co.

In *Hall GMC, Inc. v. Crane Carrier Co.*[191] the appellee, Crane, challenged the trial court's damage award.[192] The trial court awarded Hall $52,223.97 in damages for the interest Hall paid to its creditor commencing sixty days after Hall mailed its letter requesting the mutual termination of a distributorship agreement.[193]

Crane first challenged the interest award because it was not within the contemplation of the parties at the time of contracting and therefore amounted to prejudgment interest.[194] In response to Crane's first argument, the court concluded that the question of whether special damages of this sort were reasonably within the contemplation of the parties at the time of contracting was a question of fact.[195] The trial court found that at the time the parties executed the agreement Crane knew that Hall would be borrowing money from GMAC financing to cover its inventory. The finance charges, therefore, were a proper element of damages and were not prejudgment interest subject to the six percent limitation discussed in *Hirschkorn v. Severson.*[196]

Crane also argued that the court should have computed damages from 60 days after Hall's February 25. 1980, letter of unilateral cancellation rather than from the earlier January 22, 1980, letter from Hall seeking mutual termination.[197] The court relied on the specific language of the distributor agreement, which provided for termination by mutual consent of the parties at any time or unilaterally by Hall upon not less than 60 days written

189. *Id.* at 226.

190. *Id.* The court treated the issue as factual and applied the clearly erroneous rule. *Id.*

191. 332 N.W.2d 54 (N.D. 1983). See *supra* notes 39-43, 148-57 and accompanying text for a discussion of the other issues raised in *Hall GMC, Inc. v. Crane Carrier Co.*

192. Hall GMC, Inc. v. Crane Carrier Co., 332 N.W.2d 54, 56 (N.D. 1983).

193. *Id.* at 58. The interest arose because Hall had to finance its inventory of vehicles, four cement mixers, which it received from Crane. *Id.*

194. *Id.* at 62-63.

195. *Id.* at 62.

196. *Id.* at 62-63. See *supra* notes 170-78 and accompanying text for a discussion of the six percent limitation rule of *Hirschkorn v. Severson.*

197. 332 N.W.2d at 63. Crane declined to mutually terminate the distributorship after the January 22, 1980 letter. *Id.*

notice to Crane. Based on the distributor agreement the court concluded that the January 22, 1980, letter neither satisfied the legal requirements for termination nor constituted a unilateral termination of the distributorship capable of triggering the applicable 60-day time period.[198] Because the trial court's use of the January 22, 1980, letter was inappropriate, the supreme court reversed, holding that damages could not begin any sooner than 60 days after February 25, 1980, and modified the judgment to reflect this determination.[199]

The *Hall* decision illustrates the importance of drafting letters of cancellation or termination very carefully to strictly comply with the formalities prescribed by the agreement being terminated. The *Hall* case also shows how a party can avoid the six percent limitation on prejudgment interest[200] by converting interest into a special damage, reasonably contemplated by the parties at the time they execute the contract.

B. RESCISSION

1. Berg v. Hogan

In *Berg v. Hogan*[201] an auctioneer brought a breach of contract action against a high bidder who stopped payment on a check the bidder gave as a down payment.[202] The bidder argued that his bid was fraudulently inflated by bids of the seller or the seller's agents and did not form a binding contract.[203] The court indicated that when the bidder sensed that the seller was bidding up the equipment, he had the duty to find out what the true situation was and to promptly rescind or ratify the agreement.[204] Since the

198. *Id.*
199. *Id.*
200. *See* N.D. CENT. CODE § 47-14-05 (Supp. 1983). See *supra* note 172 for the text of § 47-14-05.
201. 322 N.W.2d 448 (N.D. 1982). Harry Berg conducted an auction of spraying equipment for Midstate Leasing, Inc. Berg v. Hogan, 322 N.W.2d 448, 449 (N.D. 1982). Terry Hogan was high bidder on a particular piece of equipment, but later refused to pay for it. *Id.*
202. *Id.*
203. *Id.* at 450. Section 41-02-45 of the North Dakota Century Code provides in relevant part:

> If the auctioneer knowingly receives a bid on the seller's behalf or the seller makes or procures such a bid, and notice has not been given that liberty for such bidding is reserved, the buyer may at his option avoid the sale or take the goods at the price of the last good faith bid prior to the completion of the sale. This subsection shall not apply to any bid at a forced sale.

N.D. CENT. CODE § 41-02-45 (4) (1983).
204. 322 N.W.2d at 451-52. The trial court found that Hogan first knew of the illegal bidding on May 7, 1980, the day of the auction. *Id.* at 449. The trial court also found that Hogan did not give notice of his intention to rescind until July 7, 1980. *Id.*

bidder performed acts that indicated ratification at a time when he had actual or constructive knowledge of the situation, he was not entitled to rescind the purchase.[205]

The *Berg* case indicates that even though section 9-09-04 of the North Dakota Century Code contains the phrase "and is aware of his right to rescind,"[206] the court will limit the right of rescission to cases in which a party knew or *should have known* of her right to rescind and acted promptly once she has or should have that knowledge.[207]

VII. MISCELLANEOUS

A. IMPLIED WARRANTIES

1. Koland, Inc. v. Hanggi

In *Koland, Inc. v. Hanggi*,[208] a construction case, the court reiterated the rule that an implied warranty of fitness exists when: (1) the *contractor* expressly or by implication holds itself out as competent to undertake the contract; and the *owner* (2) has no particular expertise in the kind of work contemplated; (3) furnishes no plans, designs, specifications, details, or blueprints; and (4) tacitly or expressly indicates her reliance on the experience and skill of the contractor, after making her aware of the specific purposes for which the building is intended.[209] The court also noted that the implied warranty issue is an issue of fact.[210] The court affirmed the trial court's decision, concluding that the trial court's determination of the implied warranty issue was not clearly erroneous.

B. THIRD PARTY BENEFICIARIES

1. O'Connell v. Entertainment Enterprises

The court in *O'Connell v. Entertainment Enterprises*[211] noted that

205. *Id.* at 453. Hogan's acts that indicated ratification of the contract included stating that he would pay in full, negotiating for a noncompetition agreement, and stating that he would not perform because he was unable to obtain the entire business. *Id.* at 449.

206. *See* N.D. CENT. CODE § 9-09-04(1) (1975).

207. *See* 322 N.W.2d at 452-53.

208. 320 N.W.2d 502 (N.D. 1982). Koland, Inc. contracted to build a steel building for Hanggi. Koland, Inc. v. Hanggi, 320 N.W.2d 502, 503 (N.D. 1982). Upon completion, Hanggi refused final payment because of defects in the construction. *Id.*

209. *Id.* at 506. The court first expressed the implied warranty of fitness test in Dobler v. Malloy, 214 N.W.2d 510, 516 (N.D. 1973) (implied warranty of fitness can be invoked even in situations when the contractor builds from the owner's plans).

210. 320 N.W.2d at 506.

211. 317 N.W.2d 385 (N.D. 1982). See *supra* notes 19-29 and accompanying text for a discussion of the facts in *O'Connell v. Entertainment Enterprises.*

to recover on a third party beneficiary theory, the contract the third party relied upon must be expressly made to benefit the third party.[212] On the record, the court concluded that O'Connell was merely an incidental, as opposed to an express, beneficiary of the contract he sought to enforce.[213]

The Restatement (Second) of Contracts takes a more liberal view with regard to third party beneficiaries, providing only that the beneficiary prove that she was an "intended beneficiary" of the contract.[214] Since the legislature had not opted for the more flexible or liberal approach of the Restatement, however, the court felt constrained to limit recovery under the third party beneficiary theory to those "expressly" intended to benefit from the agreement.[215] While the court may have been appropriately reticent to extend the third party beneficiary theory in light of the specific language contained in the statute, this is another area in which the legislature might be advised to reconsider its fairly inflexible stance, particularly in light of the trend toward flexibility in other areas.

VIII. CONCLUSION

An article such as this can be little more than what it purports to be — a survey. While the Article's scope was limited to contract cases arising during 1982 and the first half of 1983, it was a fairly formidable task just to summarize the cases. Nevertheless, the Article does attempt to highlight trends and on occasion, give some practical advice. As such, it is hoped that the Article will be of benefit to the practicing bar, even if it constitutes more of an introduction to the issues discussed than a scholarly discussion of those issues.

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212. O'Connell v. Entertainment Enter., 317 N.W.2d 385, 387 (N.D. 1982). The court relied on § 9-02-04 of the North Dakota Century Code, which provides: "[A] contract made expressly for the benefit of a third person may be enforced by him at any time before the parties thereto rescind it." N.D. CENT. CODE § 9-02-04 (1975).

213. 317 N.W.2d at 388.

214. RESTATEMENT (SECOND) CONTRACTS § 302 (1981). Section 302 provides:

> (1) Unless otherwise agreed between promisor and promisee, a beneficiary of a promise is an intended beneficiary if recognition of a right to performance in the beneficiary is appropriate to effectuate the intention of the parties and either
>
> (a) the performance of the promise will satisfy an obligation of the promisee to pay money to the beneficiary; or
>
> (b) the circumstances indicate that the promisee intends to give the beneficiary the benefit of the promised performance.
>
> (2) An incidental beneficiary is a beneficiary who is not an intended beneficiary.

Id.

215. 317 N.W.2d at 388.