SHOULD WE ABANDON THE CONSIDERATION REQUIREMENT?

DIFFERING VIEWS

Contracts often include a provision stating that "in consideration of the payment of $10..." But on Dec. 31, 2004, the Texas Supreme Court ruled that those entering into option contracts don't actually have to pay the stated consideration. The question presented in that case was whether section 87(1)(a) of the Restatement (Second) of Contracts should be incorporated into the common law of Texas.

A team from Jenkens & Gilchrist successfully argued that their client could enforce a real estate option even though their client admittedly did not pay the $10. Now, two DBA members share their differing views on whether or not the long-standing consideration requirement should be abandoned in contract actions generally.

The opinion for 1464-Eight, Ltd. & Millis Management Corp. v. Gail Ann Joppich, No. 03-0109, is available by visiting http://www.supreme.courts.state.tx.us/historical/2004/dec/030109.htm.

By Robert B. Gilbreath

Abandon the consideration requirement for commercial contracts? Sounds crazy, doesn't it? Well, it didn't seem crazy to Lord Mansfield back in 1765 when he suggested that a signed written contract is enough, that we don't also need proof of consideration to be convinced that a person intended to be bound by his or her promise. And apparently it didn't sound so crazy to Chief Justice Wallace Jefferson when he recently observed: "For centuries, commentators and courts have advocated the elimination of the consideration requirement altogether."

I first ran into the idea of abandoning the consideration requirement when I started preparing for oral argument in *1464-Eight, Ltd. v. Joppich*, the case in which Chief Justice Jefferson made that remark. And the more I read what the scholars have to say about getting rid of consideration, the more it made sense to me.

Joppich involved an option agreement reciting a consideration of $10. The court of appeals held that the agreement was unenforceable because there was no evidence that the $10 had ever been paid. I must be living right, however, because Section 87 of the Restatement (Second) of Contracts has a special rule just for option contracts: A recited nominal consideration need not actually be paid.

After the Texas Supreme Court set the case for oral argument, I quickly figured out that reciting the rule in Section 87 of the Restatement (Second) of Contracts would only consume about five seconds of my oral argument. So I decided to hit the books again, whereupon I learned: "Professional reactions to the doctrine of consideration have oscillated in the course of history between the extremes of complacency and disgust."

I also discovered that, in contracts, legal formalities perform two functions: (i) an evidentiary function by providing trustworthy evidence of the existence and terms of the contract; and (ii) a cautionary function, by bringing home to the parties the significance of their acts.

In the past, the cautionary function was served by the seal. But the formalities became so eroded that any written or printed symbol would suffice, and a party could simply adopt a seal already on a document. As a result, the seal was eventually abandoned in favor of the consideration requirement. Thereafter, scholars debated whether the doctrine of consideration is any better. Oliver Wendell Holmes, for example, said consideration is as much a form as a seal.

As for Section 87 of the Restatement, renowned Columbia Law Professor Allan Farnsworth opines that the drafters were attempting to make a recital of consideration as effective a formality as a seal. For his part, Professor Joseph M. Perillo, of Fordham University, condemns the Restatement's recital requirement: "Such fictional charades should not be a part of a mature legal system." This raises a good question — does the doctrine of consideration have a place in a "mature" legal system?

In the late 19th century, the bargain theory of consideration replaced the benefit/detriment theory. That's where the peppercorn came in — a peppercorn is sufficient consideration if that's what the promisee was truly bargaining for. But as Professor Farnsworth observes, the bargain theory didn't change much in the marketplace because, in the marketplace, everyone is striking a bargain.

Consideration, as Professor Perillo explains, is designed to protect promisors from their own donative promises. And common sense tells us that in a commercial transaction, there isn't much danger of donative promises. That's why some modern scholars think we should replace consideration with the rule that a contract made in furtherance of economic activity is enforceable.

This takes us back to that great Scottish jurist, Lord Mansfield, who I believe was right all along. The cautionary function of consideration is unnecessary in a commercial setting because (i) it is safe to assume that neither party was acting altruistically, and (ii) the execution of a signed writing is enough to bring home to the parties that they are entering into a binding arrangement.

March 2 marked the 300th anniversary of Lord Mansfield's birth and the 169th anniversary of the Texas Declaration of Independence. It's time for Texas to acknowledge that Lord Mansfield was right and declare its independence from the antiquated consideration requirement. HN

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by Stephen L. Baskind

Abandon the consideration requirement? Sounds crazy, because it is, even though Lord Mansfield suggested it centuries ago. Regarding Lord Mansfield, in 1788, Thomas Jefferson purportedly exclaimed: "I hold it essential in America to forbid that any English decision which has happened since the accession of Lord Mansfield to the bench, should ever be cited in a court; because, though there have come many good ones from him, yet there is so much sly poison instilled into a great part of them, that it is better to proscribe the whole." Jefferson's negative attitude toward Mansfield may have in part been influenced by the advice Mansfield apparently offered to his fellow judges: "Decide promptly, but never give any reasons. Your decisions may be right, but your reasons are sure to be wrong."

Generally, as between Thomas Jefferson and Lord Mansfield (who also upheld the absolute dominion of Great Britain over the colonies), I stand with Jefferson. I am uncertain, however, about what Jefferson thought about consideration or whether Lord Mansfield's suggestion to obviate the consideration requirement is "sly poison," so on the necessity-of-consideration point, I will stand with time-tested Texas common-law.

In case you don't remember from your first-year contracts class, this is what Texas law requires regarding proving an enforceable contract:

- To establish an enforceable contract, a party must generally prove five elements: (a) an offer, (b) an acceptance, (c) mutual assent, (d) execution and delivery of the contract with the intent it be mutual and binding, and (e) consideration (mutuality of obligations) supporting the contract.
- A contract that lacks consideration lacks mutuality of obligations and is unenforceable.
- Consideration is the bargained-for exchange of promises and consists of either the benefit to the promisor or a loss or detriment to the promissee.
- Consideration must be sufficient, and if it is stated in the contract, it is presumed to be adequate.
- If there is no consideration, a party may be able to enforce a promise under the doctrine of promissory estoppel.

These basic rules remain in place, even under "modern" contract law. Notwithstanding the criticism of some commentators regarding the consideration requirement, the Restatement continues to recognize and require it, except in limited special circumstances (such as options contracts).

One argument for doing away with the consideration requirement is an apparent concern about the value, or lack thereof, of a "peppercorn." If a peppercorn can serve as consideration for a contract, then consideration, the argument goes, cannot have much legal meaning. Certainly, I do not intend here to defend the value of a peppercorn (although most trendy restaurants seem to think that everyone wants pepper on everything, so the lowly peppercorn must be of some value). In any event, sufficiency of consideration is an issue with which the courts can deal. While it may be an area not subject to precise definition and may be fact-sensitive, so are many areas of the law (like "proximate cause" in tort law). Indeed, the Restatement suggests that using the term "sufficient consideration" is redundant, because the term "consideration," in and of itself, refers to an element of exchange which is sufficient to satisfy the legal requirement. And, when justice requires, the courts have carved out theories of contract enforcement – such as promissory estoppel – when consideration is absent.

Apparently virtually all states recognize the consideration requirement. The *Joppich* court, although accepting the view of Restatement section 87(1)(a) (which eliminates the consideration requirement for options contract), observes it is still a minority view. Even Texas Supreme Court Chief Justice Wallace Jefferson, who apparently favors the view of the modern commentators, nevertheless is unwilling at this time to reject the consideration requirement in its entirety.

We just don't need to eliminate the consideration requirement and years of well-reasoned common law. The consideration requirement will almost always be satisfied – particularly in commercial contracts absent fraud – so it will not be an impediment to contract enforcement.

If there are unique types of contracts (like options contracts or financial guaranty contracts) that should be enforced without consideration, then the courts can develop appropriate exceptions, as the *Joppich* court and the Restatement do. In any event, equitable theories such as promissory estoppel already exist in the law to prevent unjust results when consideration is absent.

So, in celebration of the 300th birthday of Lord Mansfield, let's follow Thomas Jefferson's advice and ignore Lord Mansfield's. HN

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MINORITY CLERKSHIP LUNCHEONS

Friday, June 17, at the Pavilion at the Belo Mansion. Keynote address by State Rep. Rafael Anchia. Contact bavina@dallasbar.org.