

## CHAPTER 4

### Contracts

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**§4.1. Introduction.** It has often been argued that certainty is desirable, if indeed not necessary, in that branch of the law which adjusts rights in commercial disputes. Entrepreneurs have the responsibility of weighing business risks, but, as far as possible, they should be relieved of the danger that their commercial judgments may be frustrated by some novel legal decision. There is another attractive attribute of certainty which appeals to some students of jurisprudence — it has a tendency to decrease litigation. Where the law clearly defines rights and liabilities, the commercial community can adjust its actions accordingly and disputes may often be settled by nonjudicial means.

The Uniform Commercial Code and its predecessors, the uniform acts, are prime examples of the attention given by lawmakers to clarifying the law in the commercial area. Judicial handling of commercial cases often evidences the same interest in providing established guidelines for the businessman. *Stare decisis* becomes a stronger maxim. Equity, in the broad sense of the term, is gently shoved behind a billboard advocating strict use of rules and principles so that the pure, albeit intricate, system that ties together the transactions of the business world may be assembled as pieces that are interlocked in a jigsaw puzzle. Each individual part, no matter how queerly shaped, goes to make the whole. The completed scene is the end to be attained, the parts individually having limited value and scant beauty.

But the picture is never quite complete. Imagination can indicate what it is supposed to look like since most of the pieces are in place — or are they? Has not there been a mistake? That piece there, right in the middle, which looks like consideration, certainly is correctly placed. Yet here is another of similar shape and dimension but appearing to be promissory estoppel. Certainly one can be substituted for the other. And glance at that corner over there: the pieces obviously must lie side by side but they do not fit together. The convex side of one meets the protrusions of the other so that the assembler must allow one to overlap the other. But which one is to be placed atop?

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During the 1961 SURVEY year the courts of Massachusetts dutifully performed their task of settling commercial controversies. Of those that reached the Supreme Judicial Court none indicate any strong trends nor are there any decisions which have the likelihood of being regarded as landmarks in the law. Still several are interesting enough to report herein. Some have added certainty to the law; others dealt with issues previously doubtful without shedding appreciable light on the judicial attitude in relation to their solution. Neither individually nor collectively do the cases resolve the fundamental question of contract law: Should the law shape and mold business activity or should it be content with attempting to assist parties in attaining their reasonable expectations?

**§4.2. Output contracts: Discontinuance of business: Good faith.** Output and requirements contracts have successfully weathered various attacks and gained general acceptance as enforceable agreements.<sup>1</sup> They are specifically recognized by the Uniform Commercial Code,<sup>2</sup> which provides that the rights and duties of the parties are to be governed largely by the elastic concept of good faith. Under the code provision the terms of the contract are still the preponderating determinant of the parties' obligations, but where the action of the promisor or promisee prevents the other party from realizing on his reasonable expectations, liability will result unless the action was taken in good faith.<sup>3</sup> The workability of the good faith test is evidenced by its successful application in numerous pre-code cases.<sup>4</sup> An example of its use, in the context of a particular problem inherent in all output and requirement contracts, is found in *Neofotistos v. Harvard Brewing Co.*,<sup>5</sup> which was decided during the 1961 SURVEY year.

The plaintiff in this action agreed to purchase, and the defendant to sell, all of the spent grain resulting from the defendant's production of malt beverages at its Lowell plant. The contract extended over a five-year period, and the price was to be determined bimonthly by an agreed method but in no case was to be less than a stated minimum. The contract was performed from its inception in May of 1955 until November of 1956. At this time the defendant ceased the production of malt beverages because, in its judgment, their manufacture had become unprofitable.<sup>6</sup> Subsequently the business was sold, but the

§4.2. <sup>1</sup> See Havighurst and Berman, Requirement and Output Contracts, 27 Ill. L. Rev. 1 (1932).

<sup>2</sup> Uniform Commercial Code §2-306, G.L., c. 106, §2-306.

<sup>3</sup> See Note, Requirements Contracts Under the Uniform Commercial Code, 102 U. of Pa. L. Rev. 654 (1954).

<sup>4</sup> See Mass. Code Comment to G.L., c. 106, §2-306; 1 Williston, Contracts §104(a) (3d ed. 1957).

<sup>5</sup> 341 Mass. 684, 171 N.E.2d 865 (1961).

<sup>6</sup> It was stipulated that for the year ending September 30, 1955, defendant had an operating loss of \$163,142.55 and a net loss of \$184,582.43. For the year ending September 30, 1956, the operating loss was \$183,900.60 and the net loss was \$267,502.12. *Neofotistos v. Harvard Brewing Co.*, 341 Mass. 684, 685, 171 N.E.2d 865, 866 (1961).

Lowell plant was not reopened by the purchaser. The plaintiff, alleging breach of contract, sued and recovered a jury verdict. The Supreme Judicial Court held that the defendant's motion for a directed verdict should have been granted and ordered judgment entered for the defendant.

In its opinion the Court discusses three prior Massachusetts cases: *Proctor v. Union Coal Co.*,<sup>7</sup> *Eastern Mass. St. Ry. v. Union St. Ry.*,<sup>8</sup> and *McNally v. Schell*.<sup>9</sup> The significance of the *Neofotistos* decision is better understood if viewed in the light of these decisions.

In *Proctor v. Union Coal Co.*,<sup>10</sup> the plaintiff sold land to the defendant. As part of the sales agreement the defendant promised to furnish ice from a pond on the land as required by the plaintiff for his home and business. When the land was subsequently resold and the plaintiff was unable to procure ice from the pond, suit was brought on the contract and the plaintiff was allowed to recover. To understand the dissimilarity between *Proctor* and *Neofotistos*, it should be noted that the *Proctor* case involved a requirements contract while the agreement in the *Neofotistos* case was for the defendant's output. Although the two are similar in many ways, they also differ. In the requirements contract the vendor's obligation is determined by the needs of the vendee, while in the output contract the purchaser's duty is measured by the production of the seller. Thus, in the requirements contract the vendor's obligation will vary depending upon the action of the vendee who has the power and right to alter his requirements, at least within limits. The converse is true in the output contract, as the vendee must take all of the vendor's goods.

In both the *Proctor* case, which involved a requirements contract, and the *Neofotistos* case, which involved an output contract, the defendant was the supplier. The distinction between the two cases is obvious. In *Proctor* the defendant had no discretion whatever in the amount of ice to be given to the plaintiff—he obligated himself to supply all that the plaintiff required. In *Neofotistos*, however, the quantum of the defendant's promise was to vary, under the express terms of the contract, in response to decisions made by him subsequent to the time the parties entered into the contract. It was for him to decide the extent of his obligation by deciding how much malt beverage he should produce. The vital issue in *Neofotistos*, therefore, was whether he could exercise his determinative power to its extreme by producing nothing.

*Eastern Mass. St. Ry. v. Union St. Ry.*<sup>11</sup> was neither a requirements nor output contract in the strict sense. The defendant, owner of certain railroad freight facilities, entered into an agreement with the plaintiff whereby they both were to share these facilities during a five-

<sup>7</sup> 243 Mass. 428, 137 N.E. 659 (1923).

<sup>8</sup> 269 Mass. 329, 168 N.E. 781 (1929).

<sup>9</sup> 293 Mass. 356, 199 N.E. 748 (1936).

<sup>10</sup> 243 Mass. 428, 137 N.E. 659 (1923).

<sup>11</sup> 269 Mass. 329, 168 N.E. 781 (1929).

year period. Either party had the right to revoke the agreement by giving a six-month notice. The plaintiff gave notice and then immediately discontinued freight operations, thereby eliminating its need for use of the facilities. In a suit brought by the plaintiff for a sum alleged to be the balance due under the contract while it was actually performed, the defendant's answer set up, by way of recoupment, the allegation that plaintiff had breached its contract to use the facilities.

The Court, holding that the plaintiff had failed to perform its obligations under the contract, stated:

The defendant assumed the risk of the volume of the plaintiff's business but did not assume the risk of its voluntarily giving up that business. . . . The provisions of the contract, when interpreted in the light of the circumstances and purposes to be accomplished, mean that the plaintiff was under an obligation to carry on a freight trolley business and not to stop the normal flow of business. . . . The continuation of that business was essential to the carrying out of the terms of the contract and hence an agreement to that effect is implied.<sup>12</sup>

Although the case did not involve an output contract, the tenor of the opinion is opposed to the result in *Neofotistos*. There is no clear theoretical distinction between the two cases. In both, performance of the party sought to be charged was dependent upon his continued operation of his business, but in one the Court found an implied promise not to go out of business while in the other it did not.

The last case which the Court distinguished is *McNally v. Schell*,<sup>13</sup> which also involved a contract that falls without the strict definitions of output and requirements contracts. In this case the plaintiff was hired to collect rents in a building owned by the defendant. The plaintiff promised to perform this work for five years, but there was no specific promise by the defendant to continue his employment for any stated period of time. Before the elapse of the five years, the defendant sold the building thereby making it impossible for the plaintiff to perform under the contract. It is important to look at the issue as posed by the Court: Was the agreement revocable at the pleasure of the defendant? Holding that the plaintiff could recover damages under the contract, the Court found an implied promise by the defendant "not to disable the plaintiff from their performance of services."<sup>14</sup>

Although the way in which the opinion is worded suggests that the case has applicability to requirements and output contracts, in reality it does not. The Court clearly, and correctly, considered the cases as posing only the question of whether the contract of employment was

<sup>12</sup> 269 Mass. at 332, 168 N.E. at 782.

<sup>13</sup> 293 Mass. 356, 199 N.E. 748 (1936).

<sup>14</sup> 293 Mass. at 360, 199 N.E. at 749.

terminable at the will of the defendant. Once finding, from the circumstances and terms of the agreement, that it was not, the method by which the defendant breached his promise was immaterial.

The Court in *Neofotistos* distinguished the above three cases simply on the ground that in each designated property was devoted to the purposes of the contract and that "in the particular circumstances a promise to hold the property for that use during the term of the contract was implied."<sup>15</sup> In the *Neofotistos* contract the Court found no agreement by the defendant to produce any specific amount of malt beverages at the Lowell plant. Therefore, the Court concluded that:

Since there was no express obligation for the defendant to produce, there was no implied obligation to continue production. The only implied promise that the plaintiff could reasonably assume from the contract was that the defendant would carry out its agreement in good faith and do nothing to interfere with normal production.<sup>16</sup>

Whether the *Proctor*, *McNally*, and *Eastern Mass. St. Ry.* cases are easily distinguishable, the decision of the Court in *Neofotistos* is sound. In accord with the prevailing majority rule,<sup>17</sup> it would also seem to be in agreement with the Uniform Commercial Code.<sup>18</sup>

One final comment should be made about the case and the extent of its holding. The goods to be sold under the agreement, spent grain, was a by-product of the seller's manufacturing process, and he ceased production not because the manufacture of this by-product was unprofitable, but because the operation of his plant — the purpose of which was to produce malt beverages — was showing a loss.<sup>19</sup> The case should be restricted to similar facts and not extended to cover the situation where the vendor ceases production of the product being sold under an entire output contract because that contract has itself proved a bad bargain for him. If, for instance, a contract were for the entire output of a particular product and at a fixed price, and the price of that product rose sharply during the term of the contract, the seller should not be allowed to avoid the contract by ceasing production. The risk of such an increase was a part of the bargain.<sup>20</sup>

**§4.3. Postemployment obligations: Covenants not to compete.** In

<sup>15</sup> 341 Mass. 684, 688, 171 N.E.2d 865, 868 (1961).

<sup>16</sup> 341 Mass. at 689, 171 N.E.2d at 868.

<sup>17</sup> See 1 Williston, Contracts §104A (3d ed. 1957).

<sup>18</sup> Note, 102 U. of Pa. L. Rev. 654, 659 (1954).

<sup>19</sup> In the *Neofotistos* case the defendant seller apparently protected himself against such a bad bargain. The agreement provided for a sliding price scale. *Neofotistos v. Harvard Brewing Co.*, 341 Mass. 684, 686, 171 N.E.2d 865, 866 (1961).

<sup>20</sup> Cf. Comment 2 to Uniform Commercial Code §2-306: "A shut-down by a requirements buyer for lack of orders might be permissible when a shut-down merely to curtail losses would not."

both 1959<sup>1</sup> and 1960<sup>2</sup> extensive articles appeared surveying the law governing postemployment covenants which restrict an employee's activities after the termination of the employment relationship. A third was published in 1961.<sup>3</sup> All suggested that the danger to an employer of a trusted employee's disclosing trade secrets or misusing confidential information has greatly increased under prevailing labor market conditions wherein movement of key personnel from one company to a competitor is commonplace. As if to substantiate the authors' concern, the Supreme Judicial Court considered three cases<sup>4</sup> during the 1961 SURVEY period which directly involve an employee's obligations after termination of his employment contract. Another case,<sup>5</sup> although it arose from the sale of a business rather than an employment contract, had similar overtones.

Of these cases, *New England Overall Co. v. Woltmann*<sup>6</sup> produced the longest and in some ways the most helpful opinion. The plaintiff was a family corporation that had dealt for an extended period in a specialized type of wearing apparel, the styles of which are important and vary seasonally. There were two defendants: a salesman who had been with the company for a number of years and a sales manager who was the first person from outside the family to be trusted with company secrets. The salesman originally worked under a written contract requiring him to keep secret customer lists, prices, and other matters pertaining to the business. At the time of his defection he was on an oral year-to-year contract which the Court found to contain like terms. The sales manager understood when he assumed his position that he would keep inviolate trade and business secrets.

The defendants, while still in the employ of the plaintiff corporation, set up a competing company in conjunction with a third party. A period of double-dealing followed until eventually both resigned and began to compete openly. Customer lists were taken, information relative to suppliers heretofore closely guarded by the corporation was used by the new enterprise, and both customers and suppliers of the plaintiff were solicited by the defendants on behalf of the new company. Suit was brought, which resulted in an award of damages and a decree enjoining the defendants from soliciting or communicating

§4.3. <sup>1</sup> Blake, Employee Agreements Not to Compete, 73 Harv. L. Rev. 625 (1959); Levin, Non-Competition Covenants in New England: Part I, 39 B.U.L. Rev. 482 (1959). See also Coleman and Cole, Effect of Shifting Employment in Trade Secrets, 14 Business L. 319 (1959).

<sup>2</sup> Levin, Non-Competition Covenants in New England: Part II, 40 B.U.L. Rev. 210 (1960).

<sup>3</sup> Von Kalinowski, Key Employees and Trade Secrets, 47 Va. L. Rev. 583 (1961).

<sup>4</sup> American Window Cleaning Co. of Springfield v. Cohen, 1961 Mass. Adv. Sh. 1259, 178 N.E.2d 5; New England Overall Co. v. Woltmann, 1961 Mass. Adv. Sh. 1113, 176 N.E.2d 193; Novelty Bias Binding Co. v. Shevrin, 1961 Mass. Adv. Sh. 973, 175 N.E.2d 374.

<sup>5</sup> Slate Co. v. Bikash, 1961 Mass. Adv. Sh. 1231, 177 N.E.2d 780. See also Bonneau v. Meaney, 1961 Mass. Adv. Sh. 1465, 178 N.E.2d 577.

<sup>6</sup> 1961 Mass. Adv. Sh. 1113, 176 N.E.2d 193, also noted in §5.4 *infra*.

with customers in the New England states, New York, and Pennsylvania.

The principal contention of the defendants considered by the Court was the argument that *Woolley's Laundry, Inc. v. Silva*<sup>7</sup> had established a rule for this jurisdiction that injunctive relief would be granted an employer, in absence of an express contract, only in situations involving new or secret inventions and processes or knowledge of special circumstances. In rejecting this interpretation of the *Woolley's* case, the Court stressed a part of that opinion<sup>8</sup> which indicates that the deciding factor in such litigation is whether the knowledge or information the use of which the employer is attempting to restrain is confidential. Finding this to be the test, and that the information used by the defendants was within this category, the Court upheld the injunction.

The relief granted, a decree restraining the employees from soliciting customers of their former employer, was the same that was denied in the *Woolley's* case. It is interesting that in distinguishing the *New England Overall Co.* case from it, reliance was not placed upon the possible ground that there was here an express contract not to use customer lists, but rather on the less definite concept that the information was confidential. Although the result reached by the Court appears just, it is difficult to determine what criteria the Court used to distinguish confidential from nonconfidential information. Perhaps the Court was impressed with the fact that in the *New England Overall Co.* case it appeared that the information was not readily available to the public and probably could not have been easily obtained by one outside the corporation, whereas in *Woolley's* (which involved a laundry routeman who solicited his former customers after he went into business on his own) anyone could ascertain his customers and pertinent facts about them by following him as he covered his route. Or perhaps the manner in which the employer has himself treated the information is significant; or again, the Court may have been impressed with the value of the information to the business.

Assuming that the Court's specific reaffirmation of the *Woolley's* decision and rationale<sup>9</sup> adds to the stature of that opinion, the primary importance of *New England Overall Co.* is its indication of how the former opinion is to be read. Customer information is not to be categorically denied protection in absence of a physical taking or express contract. Whether such information is confidential is to be the primary issue, and this will depend upon the facts of the case. It

<sup>7</sup> 304 Mass. 383, 23 N.E.2d 899 (1939).

<sup>8</sup> "The questions to be determined in each case are whether the knowledge or information, the use of which the employer seeks to enjoin, is confidential, and whether, if it be confidential in whole or in part, its use ought to be prevented." *Woolley's Laundry, Inc. v. Silva*, 304 Mass. 383, 389, 23 N.E.2d 899, 902 (1939).

<sup>9</sup> The Court stated that "in rejecting the defendant's contentions, we reaffirm the result and the reasoning of the *Woolley's Laundry* case." *New England Overall Co. v. Woltmann*, 1961 Mass. Adv. Sh. 1113, 1119, 176 N.E.2d 193, 198. Cf. Case Note, 29 Ky. L.J. 247 (1941).

should be noted, however, that the *New England Overall Co.* case discloses grossly improper activities by the defendants, some of which did not directly relate to the acts restrained. Whether the injunction would have been affirmed in absence of such conduct is to be seriously doubted.

The definition of confidential information in this context was also involved in *American Window Cleaning Co. of Springfield v. Cohen*.<sup>10</sup> Here the defendant had been the president and a director of the plaintiff corporation in which either he or his wife was a minority stockholder. He was deposed as president and almost immediately thereafter established a competing window cleaning service. Apparently impressed by the fact that this was a "business which could not be conducted surreptitiously,"<sup>11</sup> the Court held that the successful solicitation of regular customers of his former employer did not amount to grounds for recovery of damages. The Court said:

There is no basis . . . for a conclusion that the defendant used confidential information in soliciting the plaintiff's regular customers. Remembered information as to plaintiff's prices, the frequency of service, and the specific needs and habits of particular customers was not confidential.<sup>12</sup>

The Court then proceeded to make a fine distinction. The defendant had submitted a bid for regular service to one of the plaintiff's "irregular"<sup>13</sup> customers prior to leaving the company. He had also prepared a revision of the bid which was submitted by another employee before the defendant left. Immediately after being voted out as president, the defendant went to this irregular customer, informed him that he was establishing his own company, was shown a copy of the revised bid by the customer, and was given a contract for the service when he undercut the bid by a slight amount. This, the Court found, was an actionable wrong entitling the plaintiff to damages. The Court stated that the defendant had

appropriated to his own purposes his work done for the plaintiff. While employed, he had established a pre-contract relationship between the plaintiff and an irregular customer which in due course was likely to ripen into a contract. Knowledge of this was special corporate information. Interference with that relationship, immediately upon discharge . . . and with the use of plaintiff's bid, . . . was unfair. [Defendant], in the circumstances, in using the plaintiff's figures as his own, stood little better than if he had used a copy of the figures carried away by him.<sup>14</sup>

<sup>10</sup> 1961 Mass. Adv. Sh. 1259, 178 N.E.2d 5.

<sup>11</sup> 1961 Mass. Adv. Sh. at 1261, 178 N.E.2d at 7.

<sup>12</sup> 1961 Mass. Adv. Sh. at 1262, 178 N.E.2d at 8.

<sup>13</sup> A customer for whom work had been done two or three times during the previous five years.

<sup>14</sup> *American Window Cleaning Co. of Springfield v. Cohen*, 1961 Mass. Adv. Sh. 1259, 1264, 178 N.E.2d 5, 9.



Admitting, as the Court does,<sup>15</sup> that if the defendant had not been in the employ of the plaintiff he would have been free to use the figures disclosed to him by the customer, the opinion furnishes few clues as to why recovery was allowed. Several reasons may be surmised for the Court's decision, but none is satisfactory. It may be argued, for instance, that use of the calculations contained in the plaintiff's bid was tantamount to a physical taking of the bid itself, but the same should also be said for remembered information about customers' habits and needs. Or the theory may be advanced that the work done on the bid by the defendant became the "property"<sup>16</sup> of the plaintiff and therefore could be used only by him, but such reasoning applies with equal vigor to any beneficial contacts or good will established by the employee during his tenure irrespective of whether a firm contract or only a pre-contractual relation resulted.

Both *New England Overall Co. v. Woltmann* and *American Window Cleaning Co. of Springfield v. Cohen* indicate that the Supreme Judicial Court has a renewed interest in affording protection to that class of knowledge gained by an employee during his tenure which the Court categorizes as "confidential information." It is impossible to define or delimit the term from the opinions in these two cases, and prior decisions of the Court afford little guidance. The distinguishing characteristic of the protected class of information seems to be its inaccessibility to a competitor who has no inside connections. The *American Window Cleaning Co.* case demonstrates that this cannot be applied as a rigid test but that it is at most a flexible guide.

The third case decided by the Supreme Judicial Court during the past year in the postemployment area, *Novelty Bias Binding Co. v. Shevrin*,<sup>17</sup> presented entirely different issues. The defendant-employee had been given access to confidential information during his nine years with the plaintiff company. Over the years he had embezzled in excess of \$130,000 from the plaintiff, which led to his discharge and the commencement of criminal proceedings against him. During the criminal prosecution he agreed to restore the money taken and also to refrain from competing with the plaintiff during the following three years. Subsequently, upon his violation of the agreement not to compete, an injunction was granted restraining him from selling articles, of the type produced by the plaintiff, during the three-year period.

In attempting to reverse the decree, the defendant unsuccessfully argued that the restrictive covenant was unenforceable because it was not ancillary to an employment contract. Two separate and independent issues are raised by the defendant's contention: (1) whether the policy favoring free competition is unduly and unreasonably curtailed by the restrictions,<sup>18</sup> and (2) whether the agreement not to

<sup>15</sup> *Ibid.*

<sup>16</sup> *Cf. Di Angeles v. Scavzillo*, 287 Mass. 29, 191 N.E. 426 (1934).

<sup>17</sup> 1961 Mass. Adv. Sh. 973, 175 N.E.2d 374.

<sup>18</sup> See *Blake, Employee Agreements Not to Compete*, 73 Harv. L. Rev. 625 (1959).

compete was supported by sufficient consideration.<sup>19</sup> Usually, courts have placed little emphasis on the second of these issues. They have either found that the restrictive covenant is ancillary and necessary to a superior bargain between the parties and thus enforceable under the *Mitchel v. Reynolds*<sup>20</sup> doctrine, or they have found that the restrictive covenant was not a subordinate part of a broader contract and hence enforceable as an unreasonable restraint on trade. Where the covenant has been found ancillary, consideration flowing from the main agreement is obviously present in most cases; where the covenant is not ancillary, the courts have seldom reached the consideration question since enforcement has been denied on the broader principle.

The defendant's agreement not to compete cannot be considered ancillary to a contract with the plaintiff, whereby the plaintiff and the district attorney promise to forbear from prosecuting the criminal case. However, as the Court holds, the restrictive covenant was ancillary to a permissible transaction: the defendant's agreement to make restitution. The Court's decision that this is not an unreasonable restraint of trade is sound. If the law, through the use of criminal sanctions, could have incarcerated the defendant for his acts, it should not be held that a lesser restraint is against the public policy favoring free competition.

The Court's treatment of the applicable sections of the Restatement of Contracts is, however, far from satisfactory. Section 515 provides that, in the absence of statutory authorization or dominant social or economic justification, a restraint of trade is unreasonable and hence unenforceable under Section 514 if it "is based on a promise to refrain from competition and is not ancillary either to a contract for the transfer of good-will or other subject of property or to an existing employment or contract of employment."

It is clear that in the absence of social or economic justification the covenant sued upon in the *Novelty Bias Binding Co.* case must be held to be unenforceable if the Restatement is to be followed. The Court, however, refuses to recognize this, and attempts to avoid the section by referring to Comment *a* of the section, which reads in part:

. . . no implication is intended that all bargains that *do not* fall within these rules are *legal*. They may or may not be. Section 516 states some bargains that are reasonable and therefore legal; but there is a territory between the two Sections . . . *which is not covered by the rules stated* in either section. [Emphasis supplied.]

The Court finds that the covenant in the instant case is one which falls within the lacuna between the two sections. Note what it does to come to this conclusion. The first sentence of Comment *a* is distorted to read that "no implication is intended that bargains that *do* fall within this section are *illegal*." The Comment does not say this,

<sup>19</sup> 6 Corbin, Contracts §1395 (1951).

<sup>20</sup> 1 P. Wms. 181, 24 Eng. Rep. 347 (Q.B. 1711).

and to infer that it means this is a glaring example of reverse logic. And again, the Court, in holding that the covenant in the case falls between Sections 515 and 516, must completely overlook the fact that Section 515 specifically covers the situation. The Court would have been on firmer ground, and would have averted possible confusion, if it had simply rejected the Restatement rule as too narrow or had clearly held that there was sufficient "social justification" for its result.

Although the consideration issue is not discussed as a separate problem, the opinion hints at the fact that it may have troubled the Court. After noting the plaintiff's right to recover the money stolen in a civil action, and after inferring that the reparation agreement was an important factor in the disposition of the criminal case, the Court stated:

The defendant doubtless desired to avoid imprisonment; the plaintiff obviously desired that the good will of the businesses be protected from one who at liberty could do it immediate and grievous harm. In the circumstances disclosed, we think consideration of public policy, equity and fair dealing favor enforcement of the covenant if it is otherwise reasonable.<sup>21</sup>

The conclusion of the Court appears correct, and the above statement is not objectionable if it is directed only to the question of whether the restraint is illegal on the ground that it is opposed to policy favoring free competition. However, since the above is phrased in words of bargain and exchange, a danger arises that the inference might be drawn that the Court is holding forbearance in the criminal prosecution, either by the plaintiff or by the district attorney, to be sufficient consideration for the defendant's promise. Even in face of the statutory encouragement given reparation agreements,<sup>22</sup> the stifling of a prosecution cannot constitute good consideration.<sup>23</sup> It is proper, however, to settle or to promise to forbear from prosecuting a civil action even though this be intertwined with a criminal prosecution.<sup>24</sup> It is the plaintiff's forbearance in the civil action, if anything, that furnishes the consideration in the *Novelty Bias Binding Co.* case for the defendant's promise not to compete.

The extent of the restriction in the case is also worthy of mention. Originally, the covenant covered a twenty-eight state area in which the plaintiff transacted business. This was narrowed to twenty-six states by the trial court on the ground that in two of the states the amount of business conducted by the plaintiff was negligible. The Supreme Judicial Court affirmed the decree in whole, reiterating its prior

<sup>21</sup> *Novelty Bias Binding Co. v. Shevrin*, 1961 Mass. Adv. Sh. 973, 976, 175 N.E.2d 374, 376.

<sup>22</sup> See G.L., c. 266, §61; *id.*, c. 276, §92.

<sup>23</sup> 6 Corbin, Contracts §1421 (1951).

<sup>24</sup> *Ibid.*

rejection<sup>25</sup> of a rule which would limit the restriction to the geographical territory in which the employee worked.

*Slate Co. v. Bikash*,<sup>26</sup> the last case to be reported in this section, was an action brought to enforce a restrictive covenant given in conjunction with the sale of a business. Two of the defendants, Bikash and his wife, owned and operated a wholesale candy and tobacco business in the city of Quincy. Their son-in-law, Kaitz, had worked with them until October of 1956 when, with their financial assistance, he purchased a similar business in Boston. In August of 1957 Bikash and his wife sold their business to the plaintiff agreeing that they would not "directly or indirectly . . . engage in the wholesale candy and tobacco business . . . in a capacity where they will personally solicit, directly or indirectly, retailers for the purpose of selling at wholesale . . . nor do anything to the prejudice of the good will."

In September of 1957 Kaitz formed a new corporation and moved his operations to Quincy. Previously, during July of that year, he had offered employment to several employees of his father-in-law's company, telling them that he intended to change the location of his business. After moving to Quincy, Kaitz was successful in soliciting former customers of his father-in-law.

This action was brought on the ground that Bikash had violated his restrictive covenant not to compete. The only specific act which the plaintiff could prove in support of his case was that Bikash had assisted his son-in-law at the time Kaitz moved to Quincy by signing as a co-maker on a note given to secure additional capital for the new enterprise. Finding that no publicity had been given to this transaction, and that Bikash had not used his business acumen in assisting his son-in-law, the Court affirmed a decree adverse to the plaintiff.

The concatenated facts of the case lead to the conclusion that the plaintiff definitely made a bad bargain in purchasing the business from the Bikashes, and that the defendants may well have executed a clever plan to sell the "good will" of their business while still passing on the benefits of that good will to their son-in-law. However, the decision of the Court is sound for it is difficult to see how, or even why, relief should be granted under the facts proved by the plaintiff. There was no violation of the covenant not to compete, nor did the Bikashes themselves undermine the good will of the business. Unfortunately for the plaintiff, the son-in-law was in a favorable position to compete, but the possibility of someone's having such an advantage should have been realized prior to the purchase.

**§4.4. Notice of exercise of option.** An option bears such a close resemblance to an offer that it is often called simply an irrevocable

<sup>25</sup> See *New England Tree Expert Co. v. Russell*, 306 Mass. 504, 28 N.E.2d 997 (1940). See also *Bonneau v. Meaney*, 1961 Mass. Adv. Sh. 1465, 178 N.E.2d 577, which held a covenant not to compete for twenty years reasonable.

<sup>26</sup> 1961 Mass. Adv. Sh. 1231, 177 N.E.2d 780.

offer.<sup>1</sup> Where the promisor has received consideration for his promise not to revoke, it is said that he is disabled from withdrawing the power of acceptance given to the offeree. Professor Corbin apparently believes that the option may be more satisfactorily explained. He looks upon the promisor's primary promise to do or refrain from doing an action at the option holder's election as a contract from its very inception, performance of which is conditional upon the option holder's proper exercise of his right.<sup>2</sup> Under his view, no new contract arises when the option is exercised, the option holder's election "merely pushes an already existing contractual obligation one step further along its way, turning the duty of [the party giving the option] that was conditional . . . into a duty that is no longer so conditional."<sup>3</sup>

It may be argued that Professor Corbin's analysis is an interesting theoretical observation which has a certain fascination for those interested in legal gymnastics, but as a practical matter it is unimportant. But look for a moment at one of the cases decided during the past year, *Cities Service Oil Co. v. National Shawmut Bank*.<sup>4</sup>

The plaintiff, Cities Service, held an option to purchase land which it was leasing. The pertinent clause of the lease provided that the "tenant shall have the option during the term of this lease . . . to purchase . . . for the sum of \$17,000 . . . payable as follows . . . \$200.00 on notice of intention to exercise this option . . . , [the option to] be exercised by the tenant giving to the landlord written notice of its intention to purchase . . ." <sup>5</sup> The lease terminated on September 1, 1959. On the evening of August 31, 1959, the plaintiff mailed notice of its intent to exercise the option with a draft for \$200 from its New York City office. This arrived on September 1 and was promptly returned.

The primary issue presented to the Court was whether the option had been exercised during the term of the lease. This depended upon whether the notice was effective when mailed or when received. The Court, in holding that the notice was late, interpreted the terms of the option to imply that notice and payment of the deposit were required so that "the purchase and sale contract [would] have been completed within the lease term." <sup>6</sup> This could have been accomplished, in the

§4.4. <sup>1</sup> Simpson, Contracts §20 (1954).

<sup>2</sup> "[The promisor's] promise is from the very beginning a binding contract, his duty to [perform] being conditional on notice by [the option holder] . . . The sending of such notice . . . is not merely the acceptance of an offer; it is also the performance of a condition precedent to [the] duty of immediate performance."

<sup>3</sup> Corbin, Contracts 873 (1950).

<sup>4</sup> Id. at 875.

<sup>5</sup> 342 Mass. 108, 172 N.E.2d 104 (1961).

<sup>6</sup> Ibid.

<sup>7</sup> 342 Mass. at 111, 172 N.E.2d at 106. Although it is possible to interpret the Court's opinion as holding that a formal purchase and sales agreement was required during the term of the lease, see quote at note 11 *infra*, it is probable that the Court meant that the giving of notice and payment of the \$200 would have automatically resulted in a sufficient contract if received during the term of the lease.

Court's opinion, by sending the notice and the deposit so as to be received before the expiration of the lease.

Keeping in mind the two views of an option, namely, as an irrevocable offer and as a conditional contract, it is both interesting and beneficial to speculate on the approach taken by the Court in reaching its decision, especially since the opinion is somewhat less than clear in expressing the Court's rationale. Four avenues were available:

1. The general rule,<sup>7</sup> which may or may not apply in Massachusetts,<sup>8</sup> that an acceptance is effective upon mailing might have been rejected.

2. The acceptance upon posting rule could have been held inapplicable to option contracts on the ground that the rule is itself an exception, and should not be extended to similar but different situations.<sup>9</sup>

3. The Court could have adopted Professor Corbin's view of the option and held that the conditions to the defendant's duty to convey had not occurred.

4. The words of the option could have been examined to ascertain the manifested intent of the parties and the conclusion drawn that they had provided for the expiration of the option unless notice was received while the lease was still operative.

The importance of ascertaining the approach of the Court is that the case must take its place as authority in this jurisdiction. The decision is certain, but the applicability of the decision will vary in accord with the rationale applied by the Court. If the Court believed that this was a simple case of offer and acceptance, the case could be cited as a reaffirmation of *McCulloch v. Eagle Ins. Co.*<sup>10</sup> On the other hand, if either of the last two theories were adopted, the case has no bearing on the time an acceptance of an offer becomes effective.

It appears that the Court, influenced perhaps by the Corbin concept of the option, rested its decision on the ground that the words used in the option require receipt of notice during the term of the lease.<sup>11</sup>

<sup>7</sup> *Adams v. Lindsell*, 1 B. & Ald. 681, 106 Eng. Rep. 250 (K.B. 1818); see 1 Williston, *Contracts* §81 (3d ed. 1957).

<sup>8</sup> Compare *McCulloch v. Eagle Ins. Co.*, 1 Pick. 278 (Mass. 1822), with *Brauer v. Shaw*, 168 Mass. 198, 46 N.E. 617 (1897).

<sup>9</sup> See 3 Williston, *Contracts* §853 n.15 (rev. ed. 1936).

<sup>10</sup> 1 Pick. 278 (Mass. 1822).

<sup>11</sup> "The words in the grant of the option 'during the term of this lease or any extension or renewal thereof' modify, we think, the words which follow them, that is 'to purchase the real estate.' It is an 'option during the term . . . to purchase.' The lease sets out the agreement that in the event of prescribed action *during the term of the lease* there would arise a bilateral contract of purchase and sale. The conditions for this contract arising are the giving of notice and the payment of \$200 'on notice of intention to exercise this option.' Although the provisions as to the \$200 payment is not in the statement: 'This option shall be exercised by the Tenant giving . . . written notice of its intention to purchase,' the requirement that the payment be made 'on notice of intention' is express, and shows the intention to have a purchase and sale agreement effective upon the down payment being made, in this respect conforming to the usual practice in respect of agreements for the sale of real property." *Cities Service Oil Co. v. National Shawmut Bank*, 342 Mass. 108, 174 N.E.2d 104, 105 (1961).

Thus it seems that the question of whether an acceptance is valid upon posting is unaffected by this decision.

**§4.5. General.** Various reasons require careful selection of cases for extended discussion in this SURVEY. Several decisions which were not treated at length do appear worthy of mention.

Four such cases involved governmental contracts. In *Essex-Lincoln Garage, Inc. v. City of Boston*,<sup>1</sup> the Court denied a bill seeking rescission of a lease of a public parking facility where a change in the direction of traffic on a one-way street resulted in a diminution of business. The Court rejected the argument that continuance of the traffic pattern was an implied condition of the lease on the ground that the lease was detailed and indicated an attempt to express the entire contract of the parties. Also rejected was the plaintiff's contention that the doctrine of frustration should apply.

*McClellan Heating Supplies, Inc. v. School Building Committee of Springfield*<sup>2</sup> reiterated the Court's prior position that G.L., c. 149, §44H (which provides that sub-bids shall be rejected if incomplete) should be interpreted reasonably in light of its purpose of protecting the public. In this case a bid containing an obvious clerical error was held acceptable.

*Singarella v. City of Boston*<sup>3</sup> raised the issue of whether approval of a contract by the Mayor of Boston given before execution of the contract was sufficient to satisfy Acts of 1890, c. 418, §6, as amended by Acts of 1950, c. 216, §1.<sup>4</sup> This statute requires the mayor's approval of contracts made by city departments when the amount involved exceeds \$1000. The Court, in holding the prior approval sufficient, relied upon a literal reading of the statute and the argument that the mayor's duty to exercise his sound judgment and practical wisdom might be fulfilled as well before as after the actual execution of the contract so long as he had a full understanding of all of its terms.

*Costonis v. Medford Housing Authority*<sup>5</sup> involved a contract which provided that no change in its terms would be effective without approval of the State Housing Board. In affirming a judgment for additional expenses claimed by a modification of specification ordered by a Government employee charged with administering the contract, the Court held that the trial judge's finding that the employee had apparent authority to agree to changes was not unreasonable.

*D'Aloisio v. Morton's, Inc.*<sup>6</sup> is basically a bailments case, but it has value for the lawyer interested in contracts. The plaintiff left a fur

§4.5. 1 1961 Mass. Adv. Sh. 979, 175 N.E.2d 466.

2 341 Mass. 322, 169 N.E.2d 741 (1960).

3 342 Mass. 385, 173 N.E.2d 290 (1961).

4 The Court held that its decision would not be affected by either Acts of 1952, c. 376, §1, or Acts of 1955, c. 60, §1. These statutes were not considered applicable as no showing was made that they had been accepted by the city council. *Singarella v. City of Boston*, 342 Mass. 385, 387 n.1, 173 N.E.2d 290, 291 n.1 (1961).

5 1961 Mass. Adv. Sh. 1153, 176 N.E.2d 25.

6 342 Mass. 231, 172 N.E.2d 819 (1961).

coat with a wholly-owned subsidiary of the defendant for storage and repair. She could not herself read English, but was accompanied by her daughter, a college student, who acted for her. When she deposited the coat, the plaintiff signed a document clearly marked as a "storage receipt and contract" which, on the reverse side, limited the liability of the defendant to \$300. The coat disappeared and upon demand of its return the defendant tendered \$300. The Court held that the document was a contract, not merely a receipt; that the plaintiff was bound by its terms, even if she had not read them, by virtue of her daughter's understanding of their import; and that the limitation applied to the defendant's liability for negligence as well as its liability under the bailment contract. However, the limitation was held not to affect the defendant's liability for conversion.