

1950

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### Repository Citation

Frank Rouiller, *Contracts: Importation of Consideration From Original Agreement*, 33 Marq. L. Rev. 233 (1950).

Available at: <https://scholarship.law.marquette.edu/mulr/vol33/iss4/3>

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# COMMENTS

## CONTRACTS—IMPORTATION OF CONSIDERATION FROM ORIGINAL AGREEMENT

The modification of a contract is an alteration in the legal relationships existing between the parties thereto, wherein the basic, and hence generalized, structure of rights and duties is preserved.<sup>1</sup> The change is brought about by acts of the contracting parties which have as immediate (proximate) ends the establishment of new and the extinguishment of old, legal and social relationships.<sup>2</sup>

The typical situation which induces one or more of the parties to a contract to seek a modification is a state of affairs wherein it is felt that the results envisaged by the contract are either insufficient or frustrating for the furtherance of interests to which the contract is related. Orders for manufactured goods are constantly being modified by change in specifications as the need arises. Such a situation leads to an attempt on the part of either one or both of the contracting parties to secure from the other a change in the content of the original agreement (redefinition of rights and/or duties), in order to bring about results which would not flow from the performance of the contract as it stood. Following the modification, the conduct of the parties is re-oriented in terms of the new agreement, and the desired outcome is the normal result. Concomitantly, there is a change in legal relationships, which allows the parties to seek legal redress in the event of non-fulfillment of the modification contract.

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<sup>1</sup> "As far as legal terminology is concerned, there is of course a strict and recognized distinction between contracts which modify and those which replace. The definition of modification is an alteration which introduces new elements into the details, or cancels some of them, but leaves the general purpose and effect of the subject matter intact, while substitution is defined as something placed in a position previously occupied by another thing and conveys the idea of complete replacement. In practice, however, the distinction is much vaguer, and it is submitted, is more one of degree than of principle, modification embracing relatively slight changes, and substitution requiring fundamental changes." 158 A.L.R. 231.

<sup>2</sup> "The meaning of a social relationship may be agreed upon by mutual consent. This implies that the parties make promises covering their future behaviour, whether toward each other or toward third persons. In such cases each party then normally counts, so far as he acts rationally, in some degree on the fact that the other will orient his action to the meaning of the agreement as he (the first actor) understands it. In part, they orient their action rationally to these expectations as given facts with, to be sure, varying degrees of subjectively 'loyal' intention of doing their part. But in part also they are motivated each by the value to him of his 'duty' to adhere to the agreement in the sense in which he understands it." Parsons, *Max Weber: The Theory of Social and Economic Organization*, p. 120. Refer to p. 118 for Weber's definition of "social relationship."

Should the parties to a contract which is partly executory on both sides wish to modify it, they could adopt one of several alternative methods for meeting the requirement of consideration, which is generally held applicable to modification contracts.<sup>3</sup> The legal duties imposed by the old contract could be changed with respect to both parties in such fashion that if the duties of one party should be solely reduced, the duties for the other party would be either changed or reduced, and should the duties of one party be solely increased, i.e., obviously increased without other compensating changes, the duties for the other party would be either changed or increased. Another method, which is rather a circumvention than a meeting of the requirement for consideration (but the legal effect is the same), is the explicit rescission of the old contract, and the formation of a new one containing provisions corresponding to the provisions of the old contract as modified. In the latter case, the duties on the part of one of the parties might be altered, increased or decreased without change of the duties of the other, and the contract would still be enforceable.<sup>4</sup>

What purpose can be served by the law in requiring the formalities of the latter technique of rescission and formation of a totally distinct contract for effectuating a change in contractual duties of one party alone?<sup>5</sup> Why should failure to meet those formalities be allowed to strike down "one-sided modification agreements entered into in good faith by laymen having no knowledge nor inclination to use that formal modification procedure? The fact situations surrounding the modification procured by a modification contract and that procured by rescission of the old contract and formation of the new are so similar that one would expect the law to attach similar legal consequences to them, i.e., deem the legal relationships resulting from the acts engaged in to procure the modification to be the same. In both cases the parties seek to achieve the same goals and identical changes in legal duties.<sup>6</sup>

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<sup>3</sup> Page, *The Law of Contracts* (Cincinnati, 1920), §2461.

<sup>4</sup> Grismore, *Principles of the Law of Contracts*, §67

<sup>5</sup> "For it is absurd—save for certainty of intent—that a document reciting a rescission and recontracting should be able to accomplish what absence of this meaningless form of an intervening "rescission" may jeopardize." Llewellyn, "Common-Law Reform of Consideration. Are there Measures?," 41 *COL. L. REV.* 863 (1941).

<sup>6</sup> Modification contracts operate primarily to vary the terms of a previous agreement, terms which the parties were free to decide upon when no binding obligations existed. Before entrance into the contractual relationship, both parties were vested with a great deal of freedom with regard to the selection of

Assuming though, that the doctrine of consideration should be applicable to modification situations,<sup>7</sup> because of sound policy considerations embodied in it,<sup>8</sup> the result would not be any different from its non-application, if the pre-existing duty rule, with its logical fallacies, were not allowed to control.<sup>9</sup> Actually, an application of the definition

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terms. The conditions which gave rise to that freedom are still to a great extent present when the contract is partially executory on both sides. At such a stage of the contract, the agreement must be regarded as very much alive. The conditions which permitted freedom with respect to the selection of the content of the contract still being present to a great extent while the contract is executory, the freedom also should be present. In that fashion, the contract will be allowed to more fully perform its function of providing "a framework for well nigh every type of passing or permanent relation between individuals and groups — a framework highly adjustable, a framework which almost never accurately indicates real working relations, but which affords a rough indication around which such relations vary, an occasional guide in cases of doubt, and a norm of ultimate appeal when the relations cease in fact to work." Llewellyn, "Contracts," *Encyclopaedia of the Social Sciences*, p. 336.

<sup>7</sup> Llewellyn takes the opposite position. "Even if revocability up to the last second were sane law for initiation of other than a business-gamble type of deal, such revocability makes nonsense when applied to readjustment, as between two parties already launched into that distinct semi-joint venture going relation known as 'Contract.' There is a type of good faith called for inside the contractual scheme. . . , the arm's length stage is over when the deal has been closed, the parties are thereafter working out a team play." Llewellyn, "Common-Law Reform of Consideration," p. 873.

<sup>8</sup> The doctrine of consideration is criticized by many present day authorities. Roscoe Pound offers a substitute. "Because men are prone to overmuch talk it does not follow that promise made by businessmen in business dealings and by others as business transactions are in any wise likely to proceed from ostentation or that we should hesitate to make them as binding in law as they are in business morals. Without accepting the will theory, may we not take a suggestion from it and enforce those promises which a reasonable man in the position of the promisee would believe to have been made deliberately with intent to assume a binding relation." Pound, *Introduction to the Philosophy of Law*, P 281.

<sup>9</sup> "It is said that the obligor does only what he is legally bound to do. But the confusion arises from a failure to distinguish between legal and moral obligations. One may be morally bound to do precisely in terms as he agrees; but he is legally bound to do as a practical matter, whatever the theory may be, only what he can be compelled to do. The law does not prohibit his breach of his contract, but leaves him free to break it if he chooses, giving the other party the remedy of damages." *Frye v. Hubbell*, 74 N.H. 538, 68 Atl. 325 (1907), 17 L.R.A., (N.S.) 1197 "The only universal consequence of a legally binding promise is, that the law makes the promisor pay damages if the promised event does not come to pass. In every case it leaves him free from interference until the time for fulfillment has gone by." Holmes, *The Common Law*, p. 301. See, Kelsen, *General Theory of Law and State*, p. 45, for the statement that rules of law are "norms in which a certain sanction is made dependent upon certain conditions."

of consideration<sup>10</sup> to the facts of a typical "one-sided" modification agreement will disclose consideration.<sup>11</sup>

The promise to do that which one is already under a duty to perform in form is similar to that which defined the original undertaking. But the collocation of words constituting the verbal manifestation of the original promise, while remaining the same, takes on a new meaning when it is made to secure additional compensation or reduction in duties. The circumstances in which the new promise is made, differing from those of the old promise, effect the change in the content of the words used to manifest the previous promise. The attitude assumed with reference to future performance by the promisor made under the new conditions, is different from that originally assumed. This follows from the fact that the orientation of the individual is made with respect to a new fact situation which in part defines the attitude involved. The promisor, after an assessment of the new facts, again directs himself toward performance of his contractual duties. Assuming the new promise to have been made in good faith, the foreseeability of performance is tremendously enhanced. This new dedication to performance, with its assurance of the completion of the contractual obligations because of the new mental state of the promisor, is the consideration which is bargained for by the other party to the modification agreement.

In Wisconsin it is not necessary for those with the knowledge of the means of circumventing the requirement of consideration for modification contracts, by rescission and new formation, to resort to that highly formal process to accomplish their purposes. Those without such knowledge or the inclination to use it who enter into modification agreements in which the element of consideration (as conventionally conceived) is absent, find their expectations induced by such agreement fulfilled under Wisconsin law. The rule that the consideration from

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<sup>10</sup> If consideration be regarded as a component of the fact situation from which a legal relationship of contract is deemed to result, then its definition must have reference to factual subject matter. Consideration may be defined as those acts of an individual which are bargained for and given in exchange for a promise. Such a definition envisages the resultants of the acts, but focusses attention on the more important feature, namely, the intervention of a human actor to alter the normal course of events. Promises fall within the definition for they are the assumption of an attitude by the promisor that a certain composite of future events will ensue through his intervention or that he will bear responsibility for their non-occurrence. "The essence of a promise is that it asserts the power of the speaker's mind over the future." Gardner, "An Inquiry into the Principles of the Law of Contracts," 46 HARV. L. REV. 1 (1932).

<sup>11</sup> "The rules which hold that a promise of additional compensation is without consideration, if the promisor does or promises to do only that which he is already under a contract obligation to do, cannot be satisfactorily rested upon the ground that the promise has suffered no detriment and the promisor has

the old contract is deemed imported into the new agreement<sup>12</sup> leads to the enforcement of the modification agreement regardless of the mechanics of its formation.

Along with the abolition of the doctrine of consideration in the field of contract modification, is the elimination of the pre-existing duty rule from the same area.<sup>13</sup> Even though the modification agreement takes the form of one party again promising to do what he was already bound to do under the original agreement in exchange for an alteration in the duties (increase or change) of the other party or the reduction or change of his own duties, the agreement is enforceable. Should the parties to a contract which is partially executory on both sides regard it as expedient to bring about a change in the duties of one of the parties *alone*, an agreement to that effect is valid, and serves to modify the original contract with reference to which it was made.

"We take it to be well settled that the parties to a contract may, by *mutual agreement* (italics author's own), vary or modify its

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received no benefit, nor upon the ground that the promisee has no right to take any other course of action than to perform. In fact, no satisfactory solution of the problem can be reached upon the basis of denying that there can be under any circumstances consideration for a promise of additional compensation in such a case, but the circumstances of the particular case, or at least of the class of cases under consideration, must be considered." *Blakeslee et al v. Board of Water Com'rs of City of Hartford*, 106 Conn. 642, 139 Atl. 106, 55 A.L.R. 1319 (1927).

<sup>12</sup> The rule was necessary for decision and consideration in the conventional sense was absent in the following Wisconsin cases: *Brown v. Everhard*, 52 Wis. 205, 8 N.W. 725 (1881), *Ruege v. Gates*, 71 Wis. 634, 38 N.W. 181 (1888), *Wis. Sulphite Fibre Co. v. Jeffris Lumber Co.*, 132 Wis. 1, 111 N.W. 237 (1907), *Foley v. Marsch*, 162 Wis. 25, 154 N.W. 982 (1916), *Murray v. Hamilton Beach Manuf. Co.*, 178 Wis. 624, 190 N.W. 460 (1922), *Mollet v. Bloedorn*, 226 Wis. 83, 275 N.W. 896 (1937). The rule was necessary for decision, but consideration in the conventional sense was present in the following cases: *Buechel v. Buechel*, 65 Wis. 532, 27 N.W. 318 (1886), *Lynch v. Henry*, 75 Wis. 631, 44 N.W. 837 (1890), *Montgomery v. American Central Ins. Co.*, 108 Wis. 146, 84 N.W. 175 (1900), *Holly v. First Nat. Bank of Kenosha*, 218 Wis. 259, 260 N.W. 429 (1935). The rule was not necessary for decision in the following cases: *Miller Saw-Trimmer Co. v. Cheshire*, 172 Wis. 278, 178 N.W. 855 (1920), *Miller v. Stanish*, 202 Wis. 539, 230 N.W. 47 (1930). The rule was improperly applied or extended in the following cases: *Kelly v. Bliss*, 54 Wis. 187, 11 N.W. 488 (1882) (agreement for rescission), *Snell v. Bray*, 56 Wis. 156, 14 N.W. 14 (1882) (substitution agreement). The rule, by dicta, was held applicable in suits for specific performance. "A subsequent contact between the same parties, which was executed for the purpose of carrying out the original intention of the parties to the preceding contract, is based on the consideration for the original contract, so that specific performance will not be refused." *Miller Saw-Trimmer Co.*, p. 279. The District Court for the Western District of Wisconsin applied the rule in *Jacobs v. J. C. Penny Co.*, 74 F. Supp. 440 (1947). The most precise statement of the rule is made in *Brown v. Everhard*, p. 207 "The same consideration which existed for the old agreement, is imported into the new agreement which is substituted for it."

<sup>13</sup> Outside the field of contract modification, the pre-existing duty rule undoubtedly still applies.

terms without any new consideration therefor. In the case of a modification or change of a contract, the consideration is deemed imported into the new agreement which is substituted for it."<sup>14</sup>

An important limitation is placed upon the operation of that rule, which could readily be supposed in light of the rationale given for abolishing the requirement of consideration for modification agreements, the contract sought to be modified must be partially executory on both sides.

"A wholly executory contract for sale may be modified without a new consideration, the consideration of the new contract being deemed sufficient. If, however, the contract is complete or executed by one party, and modification thereof must be supported by a new consideration."<sup>15</sup>

In addition, the modification must occur before breach,<sup>16</sup> or the rules governing accord and satisfaction become applicable.

Within the scope of operation of the rule regarding consideration for modification contracts are those cases wherein one of the parties threatens not to perform his obligations under the original agreement unless increased compensation is promised.<sup>17</sup> This type of case brings to the forefront the possibility of undue pressure being brought by one of the parties to change his contractual duties without the exchange of a benefit. In the typical case, the promisor's agreement of increased compensation should be enforced, since his assessment of the facts led him to regard as expedient the entrance into a modification contract. Should peculiar circumstances alter the equities of the case, it would be the function of other legal doctrines to vary the result dictated by the general rule.<sup>18</sup>

<sup>14</sup> *Kelley v. Bliss*, 54 Wis. 187, 11 N.W. 488 (1882). (1882).

<sup>15</sup> *Murray v. Hamilton Beach Manuf. Co.*, 178 Wis. 624, 190 N.W. 460 (1922).

<sup>16</sup> *Bowman v. Wright*, 65 Neb. 661, 91 N.W. 580 (1902). The modification must also have reference to a pre-existing valid contract. *Skhogasky v. Ray Worth*, 139 Wis. 115, 120 N.W. 822 (1909).

<sup>17</sup> *Foley v. Marsch*, 162 Wis. 25, 154 N.W. 982 (1916), *Mollet v. Bloedorn*, 226 Wis. 83, 275 N.W. 896 (1937). Note: The determination of whether or not an anticipatory breach occurred because of the demand for additional compensation and threatened non-performance requires an analysis which proceeds independently from the question of modification. Ordinarily, no anticipatory breach accompanies the request for additional compensation, since the intention not to perform the original contract is held in abeyance pending the outcome of the negotiations for modification. The statement of the intention not to perform is conditioned on the refusal of the other party to allow a modification.

<sup>18</sup> See, Llewellyn, "Common-Law Reform of Consideration," for a presentation of the doctrine of Undue-Unfairness.

An evaluation of economic activities shows the need for legal encouragement of modification agreements which are instrumental in maintaining productive conduct entered into by virtue of the original contract as a preferable alternative to allowing cessation of such activities and recourse to the courts.<sup>19</sup> The Wisconsin rule that the consideration from the original agreement is deemed imported into the new contract operates in furtherance of that objective.

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<sup>19</sup> "Wealth in a commercial age is made up largely of promises. An important part of everyone's substance consists of advantages which others have promised to provide for or to render to him, of demands to have the advantages promised which he may assert not against the world at large but against particular individuals. Thus the individual claims to have performance of advantageous promises secured to him. He claims satisfaction of expectations created by promises and agreements. If this claim is not secured friction and waste obviously result, and unless some countervailing interest must come into account, which would be sacrificed in the process, it would seem that the individual interest in promised advantages should be secured to the full extent of what has been assured to him by the deliberate promise of another." Pound, p. 236.