

Contract Interpretation

The subject of the interpretation of written contracts is complex but hugely important. Although professors and students alike might find this material less fun than famous and amusing cases about consideration and offer-and-acceptance, it is almost surely the case that practicing lawyers will spend a lot more time both litigating and trying to anticipate interpretation problems than they will on formation issues. Yet training for this real work to come is not easy. The rules—to the extent there even are hard-and-fast rules—vary by jurisdiction. Even intra-jurisdictionally, courts are rarely wholly consistent about their approaches to interpretation and sometimes need to apply rules differently, depending on whether the case arises under the common law or the UCC. To make matters harder still, studying these cases often requires more intimate understandings of contractual context and language than is readily studied in an introductory or survey course. Finally, matters of interpretation intersect with long-standing debates between *textualists*—those who believe the best way to read contracts is to hew carefully and nearly exclusively to the four corners of the paper labeled a “contract”—and *contextualists*—those who welcome judges to look at matters outside the document to get a feel for the “real deal” which might illuminate or even supplant the “paper deal.” This debate between textualists and contextualists can also have a political valence, with political conservatives often appreciating the rigors and benefits of formalism about contracts and many political liberals (though not all!) preferring what they take to be an equity-enhancing holistic approach. Without understanding something about the theory and politics of interpretation, it is even more likely that newbies will get lost in the weeds.

With that auspicious introduction, let’s get started! Our plan will be to start with some general principles of interpretation: first by looking at “canons” of interpretation; then by laying out some standards under the UCC and the common law in some illustrative jurisdictions. We conclude the chapter with exposure to the notorious “parol evidence rule,” which is probably best thought of as a particularized approach to one especially knotty kind of extrinsic evidence outside of a final agreement that has commanded its own interpretive regime. As we’ll see, it is about as poorly named as can be (kind of like the Holy Roman Empire?), since it doesn’t really seem limited to “parol” (oral evidence), it isn’t a rule of evidence (it is considered “substantive” contract law), and it is so shot through with exceptions that it is hard to call it a rule with a straight face. But surely by now you are used to the rule/counter

A. The Interpretation/Construction Distinction and Some Rules of Thumb

Other part of this book touch on deciding which terms are in an agreement and which terms fall away for one reason or another. But deciding on the *meaning* of the terms—and what evidence one may marshal to divine those meanings—is a different project from deciding on which terms are in the agreement. Figuring out the legal meaning of written words, it won't surprise you to learn, is not a domain exclusive to contract law. Indeed, with statutes, regulations and ordinances, too, the law is often interested in understanding the meaning of legally operative words. So, the law has developed—sometimes in very approachable Latin!—some rules of thumb about how to read words that have to be interpreted.

Some of these “canons” (as these rules of thumb are known) are thought to be “best estimates” of actual meaning and some are thought to operate in a way either to create a kind of “penalty default” or otherwise promote a seemingly worthy policy objective. The former is conventionally in service of what is *interpretation* while the latter is in service of *construction*. This is not a perfectly observed dichotomy by judges and scholars, but it is generally useful to know when a canon is being deployed to approximate a meaning attributable to the parties and when a canon is seeking to do something else. It may be appropriate to limit the latter kind of rule to cases of true ambiguity or when we are in equipoise about what the parties' meaning could be because canons that promote substantive policy agenda don't really have their genesis in trying to impute a likely meaning to the words the parties chose. In any event, since all the canons—whether of interpretation or construction—are generally treated as rules of thumb and can often be defeated by another rule of thumb cutting in another direction, it is important to try to master as many canons as you can, even if it is difficult to predict how a canon battle will ultimately be resolved in any particular case. Although you might pursue careful study of more canons in statutory interpretation courses, we can introduce a few here that are broadly used throughout the law—and then one or two that have especial relevance in contract law cases.

Consider first the twin textual canons of *noscitur a sociis* and *ejusdem generis*. These are not limited to contract law and can be applied to any legal text. The first translates to “known by its associates” and the second translates to “of the same kind.” They are both tools to furnish meaning to terms that might not be self-defining. Think of a contract term that purports to furnish grooming services to “all of the buyer's animals: dogs, cats, gerbils, and birds.” Imagine that the buyer brings in a vulture and the groomer refuses to deal with it. When the

buyer sues for breach pointing to the word “birds” in the contract, a court will have to figure out whether a vulture counts for the purposes of this hypothetical contract.

Perhaps one might look up a dictionary definition of “bird” and see if the vulture qualifies; there might be a debate in such a case about whether to use a standard dictionary or a specifically zoological one. But one can also use the canon of *noscitur a sociis* to argue that the word “bird” in the list ought to be in a meaningful way *like* the words in close association, to wit, “dogs” and “cats” and “gerbils.” Using this canon, then, we might convince a court that when the groomer was contracting to groom animals, she clearly had household pets in mind, not wild birds. As you can see in this example, although we are trying to ascertain the meaning of the word “birds” from within the text, we are relying on a principle that offers us a probabilistic meaning, one that could be defeasible with other, better evidence than an old Latin rule of thumb.

Ejusdem generis is similar, though usually is utilized not to fix the meaning of a specific word in a list but to limit a general word in a series to things of the same type. So, imagine our animal groomer is contracting with people to groom “dogs, cats, hamsters, parakeets, chinchillas, and your other animals.” When someone comes in with her pet tiger, we might explain to her that the contract really doesn’t cover that: “and other animals” does not mean any old animal you happen to feel like bringing into our shop, just pets that are similar to the listed animals. That would be using the canon of *ejusdem generis* to get at the meaning of the general phrase “and other animals” by looking at listed exemplars. Both of these canons work to get at the meaning of contracts – just like you will study that they can be used, cautiously and with care, to interpret statutory language. Both are canons of *interpretation* rather than *construction* because both purport to specify the actual meaning of the parties to the contract.

Still, understand this about canons: even though they are tools for lawyers and courts to draw upon, one can’t always be sure when they will be convincing or when they will be ignored. For example, in a famous “is-a-burrito-a-sandwich” case—more formally known as *White City v. PR Restaurants, LLC*, 21 Mass. L. Rptr. 565 (Mass. Super. Ct. 2006)—a restaurant group that owned several Panera stores got into its lease with a landlord of a shopping mall that no other competitor restaurants should be allowed to take occupancy in the mall. Here is the Lease term to which the parties agreed:

Landlord agrees not to enter into a lease . . . for a bakery or restaurant reasonably expected to have annual sales of sandwiches greater than ten percent (10%) of its total sales or primarily for the sale of high quality coffees or teas,

such as, but not limited to, Starbucks, Tea-Luxe, Pete's Coffee and Tea, and Finagle a Bagle . . . The foregoing shall not apply to (i) the use of the existing, vacant free-standing building in the Shopping Center for a Dunkin Donuts-type business, or for a business serving near-Eastern food and related products, (ii) restaurants primarily for sit-down table service, (iii) a Jewish delicatessen or (iv) a KFC restaurant operating in a new building following the demolition of the existing, freestanding building.

The Landlord contracted with a Qdoba—"a Mexican-style restaurant chain that sells burritos, quesadillas, and tacos" in the "same 'fast-casual' restaurant market" as Panera—and the Panera people sued because they thought, not to put too fine a point on it, that a burrito, a quesadilla, or a taco is enough like a sandwich that a Qdoba would violate their agreement with the landlord. Before you continue, try to apply the textual canons we discussed. If you do, did the Landlord breach the contract?

Rather than applying any textual canons to the list of named restaurants or taking the list of named restaurants to help define what might count as the legally operative word "sandwich," however, the court instead chose to rely on another canon, sometimes called the *ordinary meaning canon*. It suggests that "unless a different intention is manifested, where language has a generally prevailing meaning, it is interpreted in accordance with that meaning." Restatement (Second) of Contracts § 202(3). Courts often ascertain that "generally prevailing meaning" by looking at a dictionary, which is what the court did here, to find no ambiguity in the meaning of "sandwich":

'The New Webster Third International Dictionary describes a 'sandwich' as 'two thin pieces of bread, usually buttered, with a thin layer (as of meat, cheese, or savory mixture) spread between them.' Merriam-Webster, 2002. Under this definition and as dictated by common sense, this court finds that the term 'sandwich' is not commonly understood to include burritos, tacos, and quesadillas, which are typically made with a single tortilla and stuffed with a choice filling of meat, rice, and beans. As such, there is no viable legal basis for barring [the Landlord from letting Qdoba come into the mall].

In short, dictionaries might trump or exclude the application of *noscitur a sociis* and *ejusdem generis*. Do you think that dictionaries (in this case or in general) are a good tool in ascertaining the parties' actual meaning?

In a later noteworthy “is-it-a-sandwich” case, a judge went in another direction on tacos. Finding that a deal between a developer and neighborhood association that limited shops in the plaza to “made-to-order” or “subway-style sandwiches” and excluded certain fast-food chains, an Indiana judge was willing to accept that “tacos and burritos are Mexican-style sandwiches” and that the commitment between the developer and association should not be read to be restricted to “American cuisine-style sandwiches.” This judge also listed “Greek gyros” and “Indian naan wraps” as other permissible sandwiches. *See* Tejal Rao, *Is a Taco a Sandwich? No. Yes. Well, It Depends on the Law*, N.Y. Times, May 18, 2024, at <https://www.nytimes.com/2024/05/18/dining/taco-sandwich-indiana-mexico.html>. Should the Department of Agriculture’s definition of sandwich control? *See* Department of Agriculture, Food Standards and Labeling Policy Book (2005) (defining a burrito as a “Mexican style sandwich-like product”).

Even when dictionaries are used, and even when a court prioritizes them, other canons can also sometimes help identify the relevant dictionary definition from a list of such definitions, too. They might also help you argue which is the relevant dictionary. As it happens, the Panera people drew upon precedent in which a flour tortilla qualified as “bread,” and argued that “a food product with bread and a filling is a sandwich.” The court was having none of it, however: In that precedent, the court explained, “the International Trade Court applied the commercial meaning, rather than the ordinary meaning of bread, to corn taco shells for purposes of levying tariffs. Here, the commercial meaning of ‘bread’ is inapposite where it is the ordinary meaning that is relevant when interpreting an unambiguous contractual term such as ‘sandwiches.’” Ultimately, be aware that sometimes a court will use certain canons only when some ambiguity or vagueness appears to it—but even when you have an unambiguous term, dictionaries may still call for application of the canons as ways to identify the right meaning from a range of available definitions.

A final example of a canon of interpretation that applies in contract law as well as outside it is *inclusio unius est exclusio alterius*. Roughly translated, this maxim holds that the inclusion of one thing should be taken to be a (deliberate) exclusion of something else. So, our groomer who in one part of the contract promises to groom “dogs, cats, chinchillas, and gerbils” but later in the contract promises to knit sweaters for “dogs, chinchillas, and gerbils” might be taken to be excluding cats from the sweater benefit of the agreement. It should be clear that this is a useful and reasonable way to read a text—but also that this method has its limits. When a parent tells her children that “there shall be no hitting, kicking, or punching,” it should likely be no defense when Clem bites Gersh and then recites proudly to their law professor father: *inclusio unius est exclusio alterius*.

Sometimes legal authority will itself tell you *not* to use this canon. Remember UCC § 1-302(c)? No? Here it is: “The presence in certain provisions of the UCC of the phrase ‘unless otherwise agreed,’ or words of similar import, does not imply that the effect of other provisions may not be varied by agreement under this section.” This is the UCC effectively telling you not to use the *inclusio unius* canon to find something to be a mandatory rule just because the drafters forgot to preface a provision with the mantra of “unless otherwise agreed.” It isn’t easy to know in the case of our animal groomer whether the omission of “cats” in the sweater benefit was deliberate—but *inclusio unius* might be a useful tool for the groomer who wants to get out of knitting cat sweaters under the contract—and might be a decent approximation of the meaning of the written agreement. As you can see, applying and using the canons well is art rather than science.

There are other canons of interpretation that are not in Latin but that are also efforts to help courts understand the meaning of a document. For example, “specific provisions should control or trump more general terms.” That rule also applies in statutory interpretation as it does in contract interpretation. But let’s look at some more contract-specific canons of construction that promote specific policy agendas rather than trying to figure out what language on a page probably meant for the parties. We start below with yet another Latin canon, *contra proferentem*—a principle that tells courts to construe a contract against its drafter.

WPC Enterprises, Inc. v. United States

323 F.2d 874 (Court of Claims 1963)

DAVIS, Judge.

This is a study in the toils of ambiguity. The parties put their names to a contract which, on the point crucial to this lawsuit, could reasonably be read in two conflicting fashions. Each signatory seized in its own mind upon a different one of these contradictory versions. Compounding that confusion, they discussed the issue with each other in such a way that each thought, but this time without good reason, it had obtained the other’s acquiescence in its chosen reading. The impasse became unmistakably plain when it was too late. Our task is to determine on whom should fall the risk of such mutually reinforced obscurity.

The Government set out to procure, through bids, a large number of complex generator sets — called the MD-3 set — used to calibrate the electronic systems of the B-47 and other aircraft and to start the engines when an electric starter is required. Beech Aircraft Corporation, which had previously made these elaborate devices for the Air Force on a negotiated basis, had prepared specifications and drawings of various of the component parts which the

Government acquired and incorporated in the bid invitations. Plaintiff was the low bidder, lower than Beech and another company which had also provided the sets under a negotiated contract. After a period of consideration and some discussion, the award was made to plaintiff and it performed the contract as required by the Government.

The only dispute now before us is whether five components of these generator sets had to be manufactured by (or with the authorization of) certain named companies, as the Government urges, or whether plaintiff was entitled under the contract to furnish identical components made by other firms (presumably at lower prices). After the award, defendant insisted that the products of the specified companies had to be furnished. Plaintiff complied but, claiming that this directive constituted a contractual change, sought review by the Board of Contract Appeals under the Changes and Disputes articles. The Board turned down the appeal on the ground that plaintiff had been told before the award of the defendant's position and had acquiesced.

For the five components now involved, the textual provisions of the specifications (borrowed from Beech) gave general descriptions, without naming any manufacturer; however, the drawings (also from Beech) listed the part numbers given to the item by a particular firm and declared that that manufacturer was the “approved source,” or that the component “may be purchased” from that company, or indicated “make from” a part furnished by a particular company, or simply said that the component was a certain part number of a specific firm. . . .

Each side urges that its position is sustained by the invitation as a whole — without any need to go beyond the bounds of the contractual instruments. The defendant stresses the references to specific part numbers, designated by particular fabricators, as necessarily showing that only parts made under the aegis of that manufacturer would be acceptable; this use of exact part numbers is said to be equivalent to a mandatory direction to incorporate only those very items. . . . It should have been clear, defendant concludes, that the contract called for items supplied by or through the specific companies named in the drawings. . . .

The plaintiff, on the other hand, emphasizes the lack of express mandatory language in the references to particular manufacturers for the five disputed components — in contrast to certain other components which the specifications very plainly declared “shall be” or “shall consist of” an identified part made by a named manufacturer. A command to use only materials or elements made by a specific firm is not frequent in government procurement; it can be expected to be phrased explicitly and not left to inference. Moreover, the references to particular part numbers are not read as mandatory because of a specification provision (labeled

“Identification of Parts”) which stated: “Beech and vendor part numbers will be shown on all items except those items supplied by other than Beech Aircraft Corporation or vendors to Beech. On items supplied by other than present sources Beech part numbers will be used with a suffix to indicate a different supplier.”

To plaintiff, this clause implicitly authorized the use of identical components made by other companies than those named in the Beech drawings. . . .

This summary of the opposing contentions is enough to show that no sure guide to the solution of the problem can be found within the four corners of the contractual documents. As with so many other agreements, there is something for each party and no ready answer can be drawn from the texts alone. Both plaintiff’s and defendant’s interpretations lie within the zone of reasonableness; neither appears to rest on an obvious error in drafting, a gross discrepancy, or an inadvertent but glaring gap; the arguments, rather, are quite closely in balance. It is precisely to this type of contract that this court has applied the rule that if some substantive provision of a government-drawn agreement is fairly susceptible of a certain construction and the contractor actually and reasonably so construes it, in the course of bidding or performance, that is the interpretation which will be adopted — unless the parties’ intention is otherwise affirmatively revealed. This rule is fair both to the drafters and to those who are required to accept or reject the contract as proffered, without haggling. Although the potential contractor may have some duty to inquire about a major patent discrepancy, or obvious omission, or a drastic conflict in provisions, he is not normally required (absent a clear warning in the contract) to seek clarification of any and all ambiguities, doubts, or possible differences in interpretation. The Government, as the author, has to shoulder the major task of seeing that within the zone of reasonableness the words of the agreement communicate the proper notions — as well as the main risk of a failure to carry that responsibility. If the defendant chafes under the continued application of this check, it can obtain a looser rein by a more meticulous writing of its contracts and especially of the specifications. Or it can shift the burden of ambiguity (to some extent) by inserting provisions in the contract clearly calling upon possible contractors aware of a problem-in-interpretation to seek an explanation before bidding.

If there were nothing more, the case would end here with a ruling for the plaintiff. But the defendant argues, and the Board of Contract Appeals found, that before the award was made or the contract signed the plaintiff learned the Government’s view of the disputed point and accepted that position. . . .

[W]e agree with the Trial Commissioner that (i) both parties became aware of the other's interpretation; (ii) neither acquiesced knowingly in the other's interpretation; (iii) both thought, however, that the other had acquiesced; (iv) without either having reasonable grounds for so thinking; and, finally, that (v) neither took the proper steps to clarify the pertinent terms of the transaction until after the award was made. On both sides ambiguous utterance was piled on unwarranted assumption and laced together by unspoken premise. In the end, the Government officials thought they had made it quite clear that the named manufacturers would have to be used for all components, while the plaintiff's people felt that they had successfully stood their ground at least as to these five components. Both were wholly wrong in their understanding of the other's understanding. The discussions had been one prolonged minuet of cross-purposes.

In these circumstances should the onus of the original ambiguity in the specifications still rest on the defendant? We can see no other conclusion. As the author of the defect in the drafting which led plaintiff to the reasonable supposition that it could obtain the five components elsewhere than from the named companies, the Government was under the affirmative obligation (if it wished its own view to prevail) to clarify the meaning of the contract in definitive fashion before the plaintiff was bound. It did make such an attempt, and it did reveal its own view. But when the plaintiff demurred the Government did not adequately indicate that it stood steadfast by its announced opinion. There was a fatal insufficiency in the defendant's effort to communicate to plaintiff that the contract was to be interpreted as the Government understood it. Largely because of this lapse, the plaintiff was left with the mistaken impression that the defendant, rather than insisting, would accept plaintiff's rendering of the contract. The Government, in a word, was very lax in seeing the matter through. Since the burden of clarification was the defendant's, it must bear the risk of an insufficient attempt, even though the plaintiff's obtuseness likewise contributed to the continuance of the misunderstanding. If there had been no communication by defendant to plaintiff between the receipt of the bids and the making of the award, the defendant would have had to suffer the consequences of its poorly drafted specifications. The ineffective attempt to put things right does not place the defendant in a better position. Only an adequate effort to reach the plaintiff's mind could have that result. . . .

We hold, therefore, that the defendant was wrong in demanding that only products of (or authorized by) the named manufacturers could be used for the five components. The contract did not so require. The issue of the amount of damages or recovery has not been tried and we are not called upon to pass upon any aspects of that question.

Notes and Questions

1. Did you spot the use of an *inclusio unius* argument that one of the parties offered to help the court interpret the agreement before it gave it a construction with *contra proferentem*?
2. What are the policy rules that the court offers for adopting a construction using *contra proferentem*? Should this rule apply to any drafter of any contract? Or should it be limited only to a more powerful party, like the U.S. government here? Whatever you think *WPC* itself justifies, you should know that *contra proferentem* applies quite generally to any drafter of any agreement—and has even been applied against mere sections or provisions that aren’t jointly drafted by parties to a larger agreement. *See generally* Ethan J. Leib & Steve Thel, *Contra Proferentem and the Role of the Jury in Contract Interpretation*, 87 *TEMPLE L. REV.* 773 (2015). It is true that this canon has especial application in insurance contracts and other so-called “adhesion” contracts in which policyholders and consumers get lots of boilerplate language in their contracts about which they can’t do much. But it can also apply in standard commercial agreements, too. Remember the landlord and Panera? The court invoked *contra proferentem* there against the Panera people because they drafted the agreement and didn’t themselves include a definition of “sandwich:” “As the drafter of the exclusivity clause, [Panera] did not include a definition of ‘sandwiches’ in the lease nor communicate clearly to [the landlord] during lease negotiations that it intended to treat burritos, tacos, quesadillas, and sandwiches the same.”
3. Notice that an important trigger for this canon of construction in the *WPC* case (and quite generally) is that the court concluded that “[b]oth plaintiff’s and defendant’s interpretations lie within the zone of reasonableness.” The metaphor of tie-breaking typically appears in this context. The Michigan Supreme Court, for example, held that “the rule of *contra proferentem* should be viewed essentially as a ‘tie-breaker,’ to be utilized only after all conventional means of contract interpretation . . . have been applied and found wanting.” *Klapp v. United Ins. Grp. Agency, Inc.*, 468 Mich. 459, 472 (2003).
4. Would it be appropriate to hand interpretation over to a jury when a court concludes that a contract is genuinely ambiguous? What should the division of labor be between judge and jury in this area of interpretation?
5. The court in *WPC* notes that the non-drafting party “may have some duty to inquire about a major patent discrepancy, or obvious omission, or a drastic conflict in provisions.” Does that make sense? Shouldn’t the drafting party be held to an even

higher standard when it comes to such “obvious” issues? How easy is it to know what situations fall under “regular” discrepancies and what are “patent” ones?

6. Is *contra proferentem*, at bottom, a default rule or a mandatory rule? What if a drafter of boilerplate adds to the boilerplate as follows: “Nothing in this contract shall be interpreted or construed against the drafter of this agreement or any part of it.” Should that be effective to disable a court from drawing upon the principle? Why or why not? It may surprise you to learn that this hasn’t been much litigated and seems to be an open question in many jurisdictions. How could that be?
7. Was there no argument here to split the difference between WPC and the US, since both parties seemed at some fault?
8. The issue that divided WPC and the US in this agreement seemed material. The court also thought which both parties were reasonably mistaken, at least in the beginning. Why didn’t the rule regarding misunderstanding (remember Section 20 of the Restatement and the two ships named Peerless) lead the court to say there was no meeting of the minds and therefore no contract formed here? Did the judge forget 1L contract principles?
9. There are other canons of *construction*, such as a rule that ambiguous contracts should be given “reasonable” meanings. See, e.g., *Columbia Propane, L.P. v. Wis. Gas Co.*, 661 N.W.2d 776, 787 (Wis. 2003) (“In ascertaining the meaning of a contract that is ambiguous, the more reasonable meaning should be given effect on the probability that persons situated as the parties were would be expected to contract in that way as opposed to a way which works an unreasonable result.”). The Restatement (Second) of Contracts § 207 instructs that “in choosing among the reasonable meanings of a promise or agreement or a term thereof, a meaning that serves the public interest is generally preferred.” Do you think both moves by courts to bring a normative order to ambiguous agreements is appropriate? Do either or both move us too far from what the parties actually promised each other, forcing them to live by rules that are imposed upon them by courts? Does the whole project of contract construction implicate “contract as promise”? How not?

B. The UCC’s Interpretive Regime

Sometimes legislatures attempt to make things modestly easier for courts by telling them how to give meaning to legal text. This brings an air of democratic legitimacy to the interpretive

process. The UCC, as a statute, provides courts some instructions about how to treat contracts that come within the statute (to say nothing of the interpretive regime in UCC §§ 1-103 through 1-108 about how to read the statute itself). Consider the following sections of the UCC—and a controversial case decided under the UCC regime:

§ 1-201(3). General Definitions.

“**Agreement**” . . . means the bargain of the parties in fact, as found in their language or inferred from other circumstances, including course of performance, course of dealing, or usage of trade as provided in Section 1-303.

§ 1-303. Course of Performance, Course of Dealing, and Usage of Trade.

(a) A “course of performance” is a sequence of conduct between the parties to a particular transaction that exists if: (1) the agreement of the parties with respect to the transaction involves repeated occasions for performance by a party; and (2) the other party, with knowledge of the nature of the performance and opportunity for objection to it, accepts the performance or acquiesces in it without objection.

(b) A “course of dealing” is a sequence of conduct concerning previous transactions between the parties to a particular transaction that is fairly to be regarded as establishing a common basis of understanding for interpreting their expressions and other conduct.

(c) A “usage of trade” is any practice or method of dealing having such regularity of observance in a place, vocation, or trade as to justify an expectation that it will be observed with respect to the transaction in question. The existence and scope of such a usage must be proved as facts. If it is established that such a usage is embodied in a trade code or similar record, the interpretation of the record is a question of law.

(d) A course of performance or course of dealing between the parties or usage of trade in the vocation or trade in which they are engaged or of which they are or should be aware is relevant in ascertaining the meaning of the parties’ agreement, may give particular meaning to specific terms of the agreement, and may supplement or qualify the terms of the agreement.

(e) . . . the express terms of an agreement and any applicable course of performance, course of dealing, or usage of trade must be construed whenever reasonable as consistent with each other. If such a construction is unreasonable: (1) express terms prevail over course of performance, course of dealing, and usage of trade; (2) course of performance prevails over course of dealing and usage of trade; and (3) course of dealing prevails over usage of trade.

§ 2-202. Final Written Expression: . . . Extrinsic Evidence.

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

(a) by course of dealing or usage of trade or by course of performance

Columbia Nitrogen Corp. v. Royster Co.

451 F.2d 3 (4th Cir. 1971)

BUTZNER, Chief Judge.

Columbia Nitrogen Corp. appeals a judgment in the amount of \$750,000 in favor of F. S. Royster Guano Co. for breach of a contract for the sale of phosphate to Columbia by Royster. Columbia defended on the grounds that the contract, construed in light of the usage of the trade and course of dealing, imposed no duty to accept at the quoted prices the minimum quantities stated in the contract. . . . The district court excluded the evidence about course of dealing and usage of the trade. . . . The jury found for Royster on [] the contract claim.... We hold that Columbia's proffered evidence was improperly excluded and Columbia is entitled to a new trial on the contractual issues.

I.

Royster manufactures and markets mixed fertilizers, the principal components of which are nitrogen, phosphate and potash. Columbia is primarily a producer of nitrogen, although it manufactures some mixed fertilizer. For several years Royster had been a major purchaser of Columbia's products, but Columbia had never been a significant customer of Royster. In the fall of 1966, Royster constructed a facility which enabled it to produce more phosphate than

it needed in its own operations. After extensive negotiations, the companies executed a contract for Royster's sale of a minimum of 31,000 tons of phosphate each year for three years to Columbia, with an option to extend the term. The contract stated the price per ton, subject to an escalation clause dependent on production costs.¹

¹ In pertinent part, the contract provides:

Contract made as of this 8th day of May between COLUMBIA NITROGEN CORPORATION, a Delaware corporation, (hereinafter called the Buyer) hereby agrees to purchase and accept from F. S. ROYSTER GUANO COMPANY, a Virginia corporation, (hereinafter called the Seller) agrees to furnish quantities of Diammonium Phosphate 18-46-0, Granular Triple Superphosphate 0-46-0, and Run-of-Pile Triple Superphosphate 0-46-0 on the following terms and conditions.

Period Covered by Contract—This contract to begin July 1, 1967, and continue through June 30, 1970, with renewal privileges for an additional three year period based upon notification by Buyer and acceptance by Seller on or before June 30, 1969. Failure of notification by either party on or before June 30, 1969, constitutes an automatic renewal for an additional one-year period beyond June 30, 1970, and on a year-to-year basis thereafter unless notification of cancellation is given by either party 90 days prior to June 30 of each year.

Products Supplied Under Contract

Seller agrees to provide additional quantities beyond the minimum specified tonnage for products listed above provided Seller has the capacity and ability to provide such additional quantities.

Price—In Bulk F.O.B. Cars, Royster, Florida.

Diammonium Phosphate 18-46-0	\$61.25 Per Ton
Granular Triple Superphosphate 0-46-0	\$40.90 Per Ton
Run-of-Pile Triple Superphosphate 0-46-0	\$0.86 Per Unit

Default—If Buyer fails to pay for any delivery under this contract within 30 days after Seller's invoice to Buyer and then if such invoice is not paid within an additional 30 days after the Seller notifies the Buyer of such default, then after that time the Seller may at his option defer further deliveries hereunder or take such action as in their judgment they may decide including cancellation of this contract. Any balances carried beyond 30 days will carry a service fee of $\frac{3}{4}$ of 1% per month.

Escalation—The escalation factor up or down shall be based upon the effects of changing raw material cost of sulphur, rock phosphate, and labor as follows. These escalations up or down to become effective against shipments of products covered by this contract 30 days after notification by Seller to Buyer.

Phosphate prices soon plunged precipitously. Unable to resell the phosphate at a competitive price, Columbia ordered only part of the scheduled tonnage. At Columbia's request, Royster lowered its price for diammonium phosphate on shipments for three months in 1967, but specified that subsequent shipments would be at the original contract price. Even with this concession, Royster's price was still substantially above the market. As a result, Columbia ordered less than a tenth of the phosphate Royster was to ship in the first contract year. When pressed by Royster, Columbia offered to take the phosphate at the current market price and resell it without brokerage fee. Royster, however, insisted on the contract price. When Columbia refused delivery, Royster sold the unaccepted phosphate for Columbia's account at a price substantially below the contract price.

II.

Columbia assigns error to the pretrial ruling of the district court excluding all evidence on usage of the trade and course of dealing between the parties. It offered the testimony of witnesses with long experience in the trade that because of uncertain crop and weather conditions, farming practices, and government agricultural programs, express price and quantity terms in contracts for materials in the mixed fertilizer industry are mere projections to be adjusted according to market forces.³

No verbal understanding will be recognized by either party hereto; this contract expresses all the terms and conditions of the agreement, shall be signed in duplicate and shall not become operative until approved in writing by the Seller.

³ Typical of the proffered testimony are the following excerpts:

"The contracts generally entered into between buyer and seller of materials has always been, in my opinion, construed to be the buyer's best estimate of his anticipated requirements for a given period of time. It is well known in our industry that weather conditions, farming practices, government farm control programs, change requirements from time to time. And therefore allowances were always made to meet these circumstances as they arose."

"Tonnage requirements fluctuate greatly, and that is one reason that the contracts are not considered as binding as most contracts are, because the buyer normally would buy on historical basis, but his normal average use would be per annum of any given material. Now that can be affected very decidedly by adverse weather conditions such as a drought, or a flood, or maybe governmental programs which we have been faced with for many, many years, seed grain programs. They pay the farmer not to plant. If he doesn't plant, he doesn't use the fertilizer. When the contracts are made, we do not know of all these contingencies and what they are going to be. So the contract is made for what is considered a fair estimate of his

Columbia also offered proof of its business dealings with Royster over the six-year period preceding the phosphate contract. Since Columbia had not been a significant purchaser of Royster's products, these dealings were almost exclusively nitrogen sales to Royster or exchanges of stock carried in inventory. The pattern which emerges, Columbia claimed, is one of repeated and substantial deviation from the stated amount or price, including four instances where Royster took none of the goods for which it had contracted. Columbia offered proof that the total variance amounted to more than \$500,000 in reduced sales. This experience, a Columbia officer offered to testify, formed the basis of an understanding on which he depended in conducting negotiations with Royster.

The district court held that the evidence should be excluded. It ruled that "custom and usage or course of dealing are not admissible to contradict the express, plain, unambiguous language of a valid written contract, which by virtue of its detail negates the proposition that the contract is open to variances in its terms."

A number of Virginia cases have held that extrinsic evidence may not be received to explain or supplement a written contract unless the court finds the writing is ambiguous. . . . This rule, however, has been changed by the Uniform Commercial Code which Virginia has adopted. The Code expressly states that it "shall be liberally construed and applied to promote its underlying purposes and policies," which include "the continued expansion of commercial practices through custom, usage and agreement of the parties." Va. Code Ann. § 8.1-102. The importance of usage of trade and course of dealing between the parties is shown by § 8.2-202,

requirements. And, the contract is considered binding to the extent, on him morally, that if he uses the tonnage that he will execute the contract in good faith as the buyer."

"I have never heard of a contract of this type being enforced legally. . . . Well, it undoubtedly sounds ridiculous to people from other industries, but there is a very definite, several very definite reasons why the fertilizer business is always operated under what we call gentlemen's agreements. * * *

"The custom in the fertilizer industry is that the seller either meets the competitive situation or releases the buyer from it upon proof that he can buy it at that price. . . . [T]hey will either have the option of meeting it or releasing him from taking additional tonnage or holding him to that price."

And this custom exists "regardless of the contractual provisions."

"[T]he custom was that [these contracts] were not worth the cost of the paper they were printed on."

which authorizes their use to explain or supplement a contract. The official comment states this section rejects the old rule that evidence of course of dealing or usage of trade can be introduced only when the contract is ambiguous. . . We hold, therefore, that a finding of ambiguity is not necessary for the admission of extrinsic evidence about the usage of the trade and the parties' course of dealing.

We turn next to Royster's claim that Columbia's evidence was properly excluded because it was inconsistent with the express terms of their agreement. There can be no doubt that the Uniform Commercial Code restates the well established rule that evidence of usage of trade and course of dealing should be excluded whenever it cannot be reasonably construed as consistent with the terms of the contract. Royster argues that the evidence should be excluded as inconsistent because the contract contains detailed provisions regarding the base price, escalation, minimum tonnage, and delivery schedules. The argument is based on the premise that because a contract appears on its face to be complete, evidence of course of dealing and usage of trade should be excluded. We believe, however, that neither the language nor the policy of the Code supports such a broad exclusionary rule. Section 8.2-202 expressly allows evidence of course of dealing or usage of trade to explain or supplement terms intended by the parties as a final expression of their agreement. When this section is read in light of Va. Code Ann. § 8.1-[303(e)], it is clear that the test of admissibility is not whether the contract appears on its face to be complete in every detail, but whether the proffered evidence of course of dealing and trade usage reasonably can be construed as consistent with the express terms of the agreement.

The proffered testimony sought to establish that because of changing weather conditions, farming practices, and government agricultural programs, dealers adjusted prices, quantities, and delivery schedules to reflect declining market conditions. For the following reasons it is reasonable to construe this evidence as consistent with the express terms of the contract:

The contract does not expressly state that course of dealing and usage of trade cannot be used to explain or supplement the written contract.

The contract is silent about adjusting prices and quantities to reflect a declining market. It neither permits nor prohibits adjustment, and this neutrality provides a fitting occasion for recourse to usage of trade and prior dealing to supplement the contract and explain its terms.

Minimum tonnages and additional quantities are expressed in terms of "Products Supplied Under Contract." Significantly, they are not expressed as just "Products" or as "Products

Purchased Under Contract.” The description used by the parties is consistent with the proffered testimony.

Finally, the default clause of the contract refers only to the failure of the buyer to pay for delivered phosphate. During the contract negotiations, Columbia rejected a Royster proposal for liquidated damages of \$10 for each ton Columbia declined to accept. On the other hand, Royster rejected a Columbia proposal for a clause that tied the price to the market by obligating Royster to conform its price to offers Columbia received from other phosphate producers. The parties, having rejected both proposals, failed to state any consequences of Columbia’s refusal to take delivery—the kind of default Royster alleges in this case. Royster insists that we span this hiatus by applying the general law of contracts permitting recovery of damages upon the buyer’s refusal to take delivery according to the written provisions of the contract. This solution is not what the Uniform Commercial Code prescribes. Before allowing damages, a court must first determine whether the buyer has in fact defaulted. It must do this by supplementing and explaining the agreement with evidence of trade usage and course of dealing that is consistent with the contract’s express terms. Va.Code Ann. §§ 8.1-[303(e)], 8.2-202. Faithful adherence to this mandate reflects the reality of the marketplace and avoids the overly legalistic interpretations which the Code seeks to abolish. . . .

What Columbia seeks to show is a practice of mutual adjustments so prevalent in the industry and in prior dealings between the parties that it formed a part of the agreement governing this transaction. It is not insisting on a unilateral right to modify the contract.

Nor can we accept Royster’s contention that the testimony should be excluded under the contract clause:

No verbal understanding will be recognized by either party hereto; this contract expresses all the terms and conditions of the agreement, shall be signed in duplicate, and shall not become operative until approved in writing by the Seller.

Course of dealing and trade usage are not synonymous with verbal understandings, terms and conditions. Section 8.2-202 draws a distinction between supplementing a written contract by consistent additional terms and supplementing it by course of dealing or usage of trade. Evidence of additional terms must be excluded when “the court finds the writing to have been intended also as a complete and exclusive statement of the terms of the agreement.” Significantly, no similar limitation is placed on the introduction of evidence of course of dealing or usage of trade. Indeed the official comment notes that course of dealing and usage of trade, unless carefully negated, are admissible to supplement the terms of any writing, and

that contracts are to be read on the assumption that these elements were taken for granted when the document was phrased. Since the Code assigns course of dealing and trade usage unique and important roles, they should not be conclusively rejected by reading them into stereotyped language that makes no specific reference to them. Indeed, the Code's official commentators urge that overly simplistic and overly legalistic interpretation of a contract should be shunned.

We conclude, therefore, that Columbia's evidence about course of dealing and usage of trade should have been admitted. Its exclusion requires that the judgment against Columbia must be set aside and the case retried.

Notes and Questions

1. Does the UCC basically permit people to contract for goods with a minimum guarantee clause and for the piece of paper with that guarantee to be secondary to "usage of trade"? As you can see, the UCC adopts what is sometimes called an "incorporation" strategy: the "agreement" just is the piece of paper, the courses of performance, courses of dealing, and usages of trade all read into a harmonious whole. Can you see the advantages and disadvantages of thinking of agreements this way?
2. Notice that the court draws upon some of the official comments to § 2-202 to highlight that discerning the deal that the parties had by using evidence extrinsic to the document did not require a threshold finding of ambiguity first. Comment 1(c). And it emphasized that if parties really want to make sure extrinsic evidence of the course of performance, course of dealing, and usage of trade categories are excluded from parties' agreements, they have to "carefully negate" them. Comment 2.
3. What do you think is the rationale to incorporate usage of trade into the parties' agreement? Do you feel confident that judges will be able to discern what the "real deal" is between the parties? The UCC seems to encourage judges to scratch behind the surface of the "paper deal," but how likely is the average judge who oversees many different kinds of cases to get the whole context of the "real deal"? Consider the following study:

This Article presents an empirical study of the trade usage cases decided under the Uniform Commercial Code from 1970 to 2007 [I]t shows that usages are not typically demonstrated through the introduction of the types of "objective evidence" that the strategy's defenders suggest

will reduce the risk of interpretive error . . . Rather, usages are most commonly established solely through the testimony of the parties or their employees. Expert testimony is introduced in at most 31.5% of the cases, the introduction of trade codes is rare, and there were no cases in the study in which the regularity with which a practice was observed was demonstrated through statistical evidence rather than the mere assertion of a witness.

Lisa Bernstein, *Custom in the Courts*, 110 NW. U. L. REV. 63, 63 (2015). Considering this evidence, is the game worth the candle, given how expensive litigation and discovery are? Can you better understand why there is a movement afoot to reject the UCC's incorporationist strategy and be highly formalistic about contract interpretation, encouraging parties to put all their terms on paper up front? What are the disadvantages of that "neo-formalist" approach, do you think? Is the strategy of § 2-202 ultimately to assume the costs of judicial error and litigation and related discovery will be outweighed by saving parties contracting costs at the front end?

4. Do you think the UCC permits the use of canons of interpretation and construction? At what stage of the interpretive process? Only in cases of genuine ambiguity after accounting for the listed forms of extrinsic evidence first, such as trade usage? *See* UCC § 1-103(b) ("Unless displaced by the particular provisions of the Uniform Commercial Code, the principles of law and equity, including the law merchant and the law relative to capacity to contract, principal and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake, bankruptcy, and other validating or invalidating cause supplement its provisions."). Consider *Federal Express Corp. v. Pan American World Airways*, 623 F.2d 1297 (8th Cir. 1980) in this regard:

Appellant argues that . . . New York law requires construction of ambiguities in a writing against the drafting party. It is true that New York courts have shown some tendency to do so where the party who drafted the agreement takes a position which has little support outside some verbal ambiguity. . . . But the Uniform Commercial Code specifically requires the written language of the parties' agreement to be construed consistently with applicable trade usage, and this statutory rule of construction must prevail.

5. Was the kind of “course of dealing” evidence offered in *Columbia Nitrogen* legitimate? Weren’t the buyer and seller in different positions in their prior dealings? Should that matter under § 1-303?
6. How hard is the court supposed to try to render all the listed forms of extrinsic evidence as “reasonably consistent” with one another before deciding that a “totem-pole” hierarchy from § 1-303(e)—explicit terms control course of performance which controls course of dealing which controls usage of trade—applies? Does the hierarchy make sense as a good list of priorities in the order listed? Why or why not?
7. The court states that “[t]he contract is silent about adjusting prices and quantities to reflect a declining market. It neither permits nor prohibits adjustment.” Are you convinced? Shouldn’t stating a fixed price and minimum quantity suffice?
8. Re-read § 2-202. How might it interact with about § 2-207 (the “battle of the forms” provision) and § 2-201 (the “statute of frauds” provision)?

C. Common Law Interpretation

Below you will be introduced to excerpts from two very famous cases of interpretation in succession, one from New York’s highest court and one from California’s. These two jurisdictions are sometimes painted as two differentiated interpretive regimes. It shouldn’t be hard to see why.

W.W.W. Associates, Inc. v. Giancontieri

566 N.E.2d 639 (N.Y. Court of Appeals 1990)

KAYE, Judge.

In this action for specific performance of a contract to sell real property, the issue is whether an unambiguous reciprocal cancellation provision should be read in light of extrinsic evidence, as a contingency clause for the sole benefit of plaintiff purchaser, subject to its unilateral waiver. Applying the principle that clear, complete writings should generally be enforced according to their terms, we reject plaintiff’s reading of the contract and dismiss its complaint.

Defendants, owners of a two-acre parcel in Suffolk County, on October 16, 1986 contracted for the sale of the property to plaintiff, a real estate investor and developer. The purchase price was fixed at \$750,000—\$25,000 payable on contract execution, \$225,000 to be paid in cash on

closing (to take place “on or about December 1, 1986”), and the \$500,000 balance secured by a purchase-money mortgage payable two years later.

The parties signed a printed form Contract of Sale, supplemented by several of their own paragraphs. . . . Paragraph 31, one of the provisions the parties added to the contract form, reads: “The parties acknowledge that Sellers have been served with process instituting an action concerned with the real property which is the subject of this agreement. In the event the closing of title is delayed by reason of such litigation it is agreed that closing of title will in a like manner be adjourned until after the conclusion of such litigation provided, *in the event such litigation is not concluded, by or before 6-1-87 either party shall have the right to cancel this contract whereupon the down payment shall be returned and there shall be no further rights hereunder.*” (Emphasis supplied.) . . .

The Contract of Sale, in other paragraphs the parties added to the printed form, provided that the purchaser alone had the unconditional right to cancel the contract within 10 days of signing (para 32), and that the purchaser alone had the option to cancel if, at closing, the seller was unable to deliver building permits for 50 senior citizen housing units (para 29).

The contract in fact did not close on December 1, 1986, as originally contemplated. As June 1, 1987 neared, with the litigation still unresolved, plaintiff on May 13 wrote defendants that it was prepared to close and would appear for closing on May 28; plaintiff also instituted the present action for specific performance. On June 2, 1987, defendants canceled the contract and returned the down payment, which plaintiff refused. Defendants thereafter sought summary judgment dismissing the specific performance action, on the ground that the contract gave them the absolute right to cancel.

Plaintiff's claim to specific performance rests upon its recitation of how paragraph 31 originated. . . . Critical to the success of plaintiff's position is consideration of the extrinsic evidence that paragraph 31 was added to the contract solely for its benefit.

[But] before looking to evidence of what was in the parties' minds, a court must give due weight to what was in their contract.

A familiar and eminently sensible proposition of law is that, when parties set down their agreement in a clear, complete document, their writing should as a rule be enforced according to its terms. Evidence outside the four corners of the document as to what was really intended but unstated or misstated is generally inadmissible to add to or vary the writing. That rule imparts “stability to commercial transactions by safeguarding against fraudulent claims,

perjury, death of witnesses ... infirmity of memory ... [and] the fear that the jury will improperly evaluate the extrinsic evidence.” Such considerations are all the more compelling in the context of real property transactions, where commercial certainty is a paramount concern.

Whether or not a writing is ambiguous is a question of law to be resolved by the courts. In the present case, the contract, read as a whole to determine its purpose and intent plainly manifests [that the defendant’s position is correct]. Thus, we conclude there is no ambiguity as to the cancellation clause in issue, read in the context of the entire agreement, and that it confers a reciprocal right on both parties to the contract.

The question next raised is whether extrinsic evidence should be considered in order to create an ambiguity in the agreement. That question must be answered in the negative. It is well settled that “extrinsic evidence . . . is not admissible to create an ambiguity in a written agreement which is complete and clear and unambiguous upon its face.” By ignoring the plain language of the contract, plaintiff effectively rewrites the bargain that was struck. An analysis that begins with consideration of extrinsic evidence of what the parties meant, instead of looking first to what they said and reaching extrinsic evidence only when required to do so because of some identified ambiguity, unnecessarily denigrates the contract and unsettles the law.

Pacific Gas & Elec. Co. v. G.W. Thomas Drayage Co.

442 P.2d 641 (Supreme Court of California 1968)

TRAYNOR, Chief Justice.

Defendant appeals from a judgment for plaintiff in an action for damages for injury to property under an indemnity clause of a contract.

In 1960 defendant entered into a contract with plaintiff to furnish the labor and equipment necessary to remove and replace the upper metal cover of plaintiff’s steam turbine. Defendant agreed to perform the work ‘at [its] own risk and expense’ and to ‘indemnify’ plaintiff ‘against all loss, damage, expense and liability resulting from ... injury to property, arising out of or in any way connected with the performance of this contract.’ Defendant also agreed to procure not less than \$50,000 insurance to cover liability for injury to property. Plaintiff was to be an additional named insured, but the policy was to contain a cross-liability clause extending the coverage to plaintiff’s property.

During the work the cover fell and injured the exposed rotor of the turbine. Plaintiff brought this action to recover \$25,144.51, the amount it subsequently spent on repairs. During the trial it dismissed a count based on negligence and thereafter secured judgment on the theory that the indemnity provision covered injury to all property regardless of ownership.

Defendant offered to prove by admissions of plaintiff's agents, by defendant's conduct under similar contracts entered into with plaintiff, and by other proof that in the indemnity clause the parties meant to cover injury to property of third parties only and not to plaintiff's property. Although the trial court observed that the language used was 'the classic language for a third party indemnity provision' and that 'one could very easily conclude that ... its whole intendment is to indemnify third parties,' it nevertheless held that the 'plain language' of the agreement also required defendant to indemnify plaintiff for injuries to plaintiff's property. Having determined that the contract had a plain meaning, the court refused to admit any extrinsic evidence that would contradict its interpretation.

When the court interprets a contract on this basis, it determines the meaning of the instrument in accordance with the 'extrinsic evidence of the judge's own linguistic education and experience.' (3 Corbin on Contracts (1960 ed.)) The exclusion of testimony that might contradict the linguistic background of the judge reflects a judicial belief in the possibility of perfect verbal expression. This belief is a remnant of a primitive faith in the inherent potency and inherent meaning of words. The test of admissibility of extrinsic evidence to explain the meaning of a written instrument is not whether it appears to the court to be plain and unambiguous on its face, but whether the offered evidence is relevant to prove a meaning to which the language of the instrument is reasonably susceptible.

A rule that would limit the determination of the meaning of a written instrument to its four-corners merely because it seems to the court to be clear and unambiguous, would either deny the relevance of the intention of the parties or presuppose a degree of verbal precision and stability our language has not attained.

Some courts have expressed the opinion that contractual obligations are created by the mere use of certain words, whether or not there was any intention to incur such obligations. Under this view, contractual obligations flow, not from the intention of the parties but from the fact that they used certain magic words. Evidence of the parties' intention therefore becomes irrelevant.

In this state, however, the intention of the parties as expressed in the contract is the source of contractual rights and duties. A court must ascertain and give effect to this intention by

determining what the parties meant by the words they used. Accordingly, the exclusion of relevant, extrinsic, evidence to explain the meaning of a written instrument could be justified only if it were feasible to determine the meaning the parties gave to the words from the instrument alone. If words had absolute and constant referents, it might be possible to discover contractual intention in the words themselves and in the manner in which they were arranged. Words, however, do not have absolute and constant referents. ‘A word is a symbol of thought but has no arbitrary and fixed meaning like a symbol of algebra or chemistry, ...’ The meaning of particular words or groups of words varies with the ‘verbal context and surrounding circumstances and purposes in view of the linguistic education and experience of their users and their hearers or readers (not excluding judges). ... A word has no meaning apart from these factors; much less does it have an objective meaning, one true meaning’ [citing Corbin]. ...

Although extrinsic evidence is not admissible to add to, detract from, or vary the terms of a written contract, these terms must first be determined before it can be decided whether or not extrinsic evidence is being offered for a prohibited purpose. The fact that the terms of an instrument appear clear to a judge does not preclude the possibility that the parties chose the language of the instrument to express different terms. That possibility is not limited to contracts whose terms have acquired a particular meaning by trade usage,⁶ but exists whenever the parties’ understanding of the words used may have differed from the judge’s understanding.

Accordingly, rational interpretation requires at least a preliminary consideration of all credible evidence offered to prove the intention of the parties.⁷ Such evidence includes testimony as

⁶ [In previous decisions of courts in California] extrinsic evidence of trade usage or custom has been admitted to show that the term ‘United Kingdom’ in a motion picture distribution contract included Ireland; that the word ‘ton’ in a lease meant a long ton or 2,240 pounds and not the statutory ton of 2,000 pounds; that the word ‘stubble’ in a lease included not only stumps left in the ground but everything ‘left on the ground after the harvest time;’ that the term ‘north’ in a contract dividing mining claims indicated a boundary line running along the ‘magnetic and not the true meridian;’ and that a form contract for purchase and sale was actually an agency contract.

⁷ When objection is made to any particular item of evidence offered to prove the intention of the parties, the trial court may not yet be in a position to determine whether in the light of all of the offered evidence, the item objected to will turn out to be admissible as tending to prove a meaning of which the language of the instrument is reasonably susceptible or inadmissible as tending to prove a meaning of which the language is not reasonably

to the circumstances surrounding the making of the agreement ... including the object, nature and subject matter of the writing so that the court can place itself in the same situation in which the parties found themselves at the time of contracting. If the court decides, after considering this evidence, that the language of a contract, in the light of all the circumstances, is fairly susceptible of either one of the two interpretations contended for extrinsic evidence relevant to prove either of such meanings is admissible.⁸

In the present case the court erroneously refused to consider extrinsic evidence offered to show that the indemnity clause in the contract was not intended to cover injuries to plaintiff's property. Although that evidence was not necessary to show that the indemnity clause was reasonably susceptible of the meaning contended for by defendant, it was nevertheless relevant and admissible on that issue. Moreover, since that clause was reasonably susceptible of that meaning, the offered evidence was also admissible to prove that the clause had that meaning and did not cover injuries to plaintiff's property. Accordingly, the judgment must be reversed.

Notes and Questions

1. One might say that rather than two differentiated interpretive regimes (or three if the UCC is distinct from both New York and California), there is really a continuum of interpretation on display here. The most exclusionary regime would be a strict "four corners" approach, all of the time; then mostly text with a hint of context; then a preference for context to help refract the text; then finally an approach that really sought to use plain meaning only as a backstop when other tools of divining the reasonable intent of the parties from context and extrinsic evidence runs out. Where are New York, California, and the UCC on this continuum, do you think? Take a quick look at the International Institute for the Unification of Private Law (UNIDROIT), which has articulated principles of contract interpretation for international contracts that opt-in to its interpretive regime: <https://www.unidroit.org/english/principles/contracts/principles2016/principles2016-e.pdf> (chapter 4). How would you characterize these principles on the continuum

susceptible. In such case the court may admit the evidence conditionally by either reserving its ruling on the objection or by admitting the evidence subject to a motion to strike.

⁸ Extrinsic evidence has often been admitted in such cases on the stated ground that the contract was ambiguous. This statement of the rule is harmless if it is kept in mind that the ambiguity may be exposed by extrinsic evidence that reveals more than one possible meaning.

just mentioned? Although these principles are not law in the United States unless parties embrace them, do they provide perspective on what the law actually is in US jurisdictions?

2. Might everything turn on ambiguity, in the final analysis? Isn't even New York willing to admit extrinsic evidence once it makes a determination about contract language ambiguity? Consider this famous case, decided under New York law (shortly before the state adopted the UCC) by a famous judge from the Second Circuit, Henry Friendly (who was sitting on the trial court in the Southern District of New York for this case):

The issue is, what is chicken? Plaintiff says "chicken" means a young chicken, suitable for broiling and frying. Defendant says "chicken" means any bird of that genus that meets contract specifications on weight and quality, including what it calls "stewing chicken" and plaintiff pejoratively terms "fowl." Dictionaries give both meanings, as well as some others not relevant here. To support its, plaintiff sends a number of volleys over the net; defendant essays to return them and adds a few serves of its own. . . .

Since the word "chicken" standing alone is ambiguous, I turn first to see whether the contract itself offers any aid to its interpretation. Plaintiff says the 1½-2 lbs. birds necessarily had to be young chicken since the older birds do not come in that size, hence the 2½-3 lbs. birds must likewise be young. This is unpersuasive as a contract for "apples" of two different sizes could be filled with different kinds of apples even though only one species came in both sizes. Defendant notes that the contract called not simply for chicken but for "US Fresh Frozen Chicken, Grade A, Government Inspected." It says the contract thereby incorporated by reference the Department of Agriculture's regulations, which favor its interpretation; I shall return to this after reviewing plaintiff's other contentions.

Plaintiff's next contention is that there was a definite trade usage that "chicken" meant "young chicken." Defendant showed that it was only beginning in the poultry trade in 1957, thereby bringing itself within the principle that "when one of the parties is not a member of the trade or other circle, his acceptance of the standard must be made to appear" by proving either that he had actual knowledge of the usage or that the

usage is “so generally known in the community that his actual individual knowledge of it may be inferred.” Here there was no proof of actual knowledge of the alleged usage; indeed, it is quite plain that defendant’s belief was to the contrary. In order to meet the alternative requirement, the law of New York demands a showing that “the usage is of so long continuance, so well established, so notorious, so universal and so reasonable in itself, as that the presumption is violent that the parties contracted with reference to it, and made it a part of their agreement.” . . .

Defendant’s witness Weininger, who operates a chicken eviscerating plant in New Jersey, testified “Chicken is everything except a goose, a duck, and a turkey. Everything is a chicken, but then you have to say, you have to specify which category you want or that you are talking about.” Its witness Fox said that in the trade “chicken” would encompass all the various classifications. Sadina, who conducts a food inspection service, testified that he would consider any bird coming within the classes of “chicken” in the Department of Agriculture’s regulations to be a chicken. The specifications approved by the General Services Administration include fowl as well as broilers and fryers under the classification “chickens.” Statistics of the Institute of American Poultry Industries use the phrases “Young chickens” and “Mature chickens,” under the general heading “Total chickens” and the Department of Agriculture’s daily and weekly price reports avoid use of the word “chicken” without specification.

Defendant advances several other points which it claims affirmatively support its construction. Primary among these is the regulation of the Department of Agriculture, 7 C.F.R. § 70.300-70.370, entitled, “Grading and Inspection of Poultry and Edible Products Thereof” and in particular § 70.301 which recited: “Chickens. The following are the various classes of chickens: (a) Broiler or fryer . . . ; (b) Roaster . . . ; (c) Capon . . . ; (d) Stag . . . ; (e) Hen or stewing chicken or fowl . . . ; (f) Cock or old rooster . . .”

. . . [T]here is force in defendant’s argument that the contract made the regulations a dictionary, particularly since the reference to Government grading was already in plaintiff’s initial cable. . . .

When all the evidence is reviewed, it is clear that defendant believed it could comply with the contracts by delivering stewing chicken in the 2½-3 lbs. size. Defendant's subjective intent would not be significant if this did not coincide with an objective meaning of "chicken." Here it did coincide with one of the dictionary meanings, with the definition in the Department of Agriculture Regulations to which the contract made at least oblique reference, with at least some usage in the trade...

Plaintiff has the burden of showing that 'chicken' was used in the narrower rather than in the broader sense, and this it has not sustained . . . Judgment shall be entered dismissing the complaint with costs

Frigaliment Importing Co. v. B.N.S. International Sales Corp., 190 F. Supp. 116 (S.D.N.Y. 1960) (applying New York law). Obviously, today a contract for the sale of "chickens" would come within the UCC. Would the case be approached differently thereunder? Are the arguments from "usage of trade" consistent with what an argument under UCC § 1-303 should look like? Generally, the use of course of performance, course of dealing, and usage of trade is not limited to the sale of goods. See, e.g., Restatement (Second) of Contracts § 202(5). Is *Frigaliment* consistent with the approach of the New York Court of Appeals in *W.W.W.* (even though *Frigaliment* preceded *W.W.W.*)? More generally, the UCC is now the law in both New York and California, of course. In cases within the UCC, how might a jurisdiction committed to the "four corners" of the text implement its preferences? And what happened to the misunderstanding rule (the two ships named 'Peerless' and section 20 of the Restatement) in the *Frigaliment* case?

3. At the very least, what a court may look at to make a threshold determination about ambiguity (always treated as a question of law for the judge and as reviewable *de novo* appeal) seems to differ between New York and California, right? Review those footnotes again from *Pacific Gas* before answering. Some courts try to have it both ways: they will admit that they are "not unmindful of the dangers of focusing only upon the words of the writing in interpreting an agreement" and that "whether the language of an agreement is clear and unambiguous may not be apparent without cognizance of the context in which the agreement arose"—yet still double-down on adherence to "plain meaning," seeking to exclude extrinsic evidence. *Stewart v. McChesney*, 489 Pa. 45, 444 A.2d 659 (1982).

4. Does interpreting contractual language in accordance with its “plain meaning” preclude what one might call “purposive” interpretation, which allows a court to read the language of a contract by giving it the most reasonable meaning in light of the clear purpose of the contract? See *Spaulding v. Morse*, 322 Mass. 149, 76 N.E. 2d 137 (1947) (reading a support and maintenance provision of a divorce contract purposively to allow an ex-spouse not to pay the increased support amount for higher education of his son when the son was enlisted in the Armed Service after high school and before college). Will this depend where on the continuum of interpretation a jurisdiction finds itself?
5. Compare the policy justifications in both opinions. In *W.W.W.* the New York Court of Appeals, stated that “[b]y ignoring the plain language of the contract, plaintiff [who asked to introduce extrinsic evidence] effectively rewrites the bargain that was struck. [That approach] unnecessarily denigrates the contract and unsettles the law.” In *Pacific Gas* the California Supreme Court explained that “[a] rule that would limit the determination of the meaning of a written instrument to its four-corners . . . would either deny the relevance of the intention of the parties or presuppose a degree of verbal precision and stability our language has not attained . . . the intention of the parties as expressed in the contract is the source of contractual rights and duties.” Does the NY approach protect “the bargain that was struck” or the CA one preserve “the intention of the parties”? Could both be true? Does “the contract” mean the same thing to those courts? What interests do each approach promote?
6. We so far considered what the California Supreme Court in *Pacific Gas* instructed judges to do. It might be worthwhile to try and separate that discussion from Chief Justice Traynor’s views that words lack “absolute and constant” meaning. That is likely the most debated and controversial part of the opinion and has been pilloried by some as embracing too much relativism about word meaning (and Traynor’s strong language, including calling the opposite view a “primitive faith,” probably did not help in making the disagreement more refined and less visceral). But if we instead focus on the rule that the California Supreme Court formulated, isn’t there something of a “plain meaning” idea still left within the *Pacific Gas* articulation of what kinds of evidence would be excluded from going to the jury?
7. With the previous point in mind, was the Ninth Circuit’s gloss on *Pacific Gas* apt in *Trident Center v. Connecticut General Life Insurance Co.*, 847 F.2d 564 (9th Cir. 1988) (Kozinski, C.J.) below:

Under *Pacific Gas*, it matters not how clearly a contract is written . . . nor how carefully it is negotiated, nor how squarely it addresses the issue before the court: the contract cannot be rendered impervious to attack by [extrinsic] evidence. If one side is willing to claim that the parties intended one thing but the agreement provides for another, the court must consider extrinsic evidence of possible ambiguity. If that evidence raises the specter of ambiguity where there was none before, the contract language is displaced and the intention of the parties must be divined from self-serving testimony offered by partisan witnesses whose recollection is hazy from passage of time and colored by their conflicting interests. We question whether this approach is more likely to divulge the original intention of the parties than reliance on the seemingly clear words they agreed upon at the time.

Pacific Gas casts a long shadow of uncertainty over all transactions negotiated and executed under the law of California. As this case illustrates, even when the transaction is very sizeable, even if it involves only sophisticated parties, even if it was negotiated with the aid of counsel, even if it results in contract language that is devoid of ambiguity, costly and protracted litigation cannot be avoided if one party has a strong enough motive for challenging the contract. While this rule creates much business for lawyers and an occasional windfall to some clients, it leads only to frustration and delay for most litigants and clogs already overburdened courts.

It also chips away at the foundation of our legal system. By giving credence to the idea that words are inadequate to express concepts, *Pacific Gas* undermines the basic principle that language provides a meaningful constraint on public and private conduct. . . . Be that as it may. While we have our doubts about the wisdom of *Pacific Gas*, we have no difficulty understanding its meaning, even without extrinsic evidence to guide us. As we read the rule in California, we must reverse and remand to the district court in order to give plaintiff an opportunity to present extrinsic evidence as to the intention of the parties in drafting the contract. It may not be a wise rule we are applying, but it is a rule that binds us.

Is this a good reading of *Pacific Gas*? The *Trident* case was about a contract for a \$56 million commercial loan over a 15-year period and the borrower read the contract to provide an option to prepay at any time, if it was willing to pay the prepayment fee. But the promissory note read that the borrower “shall not have the right to prepay the principal amount hereof in whole or in part” for the first 12 years. However, the note continues, in the event of default during the first 12 years, the lender could accelerate the note and add a 10 percent prepayment fee. Could Kozinski have applied *Pacific Gas* faithfully and still excluded the extrinsic evidence of the borrower’s preferred meaning? Why or why not?

8. Do you sense from the *Trident* excerpt you read a political or ideological battle being waged? The *Wall Street Journal* celebrated *Trident*’s criticism of California’s interpretive regime. Why might where one finds oneself on the interpretive continuum be a modest predictor of where one is on the political spectrum, with Republican and conservative judges usually preferring more formalist or textualist regimes, whereas more liberal hippies prefer contextualist interpretation? To be fair, however, this is just rough correlation: plenty of political liberals in the judiciary and the academy like formalistic rules for big companies on presumptively law & economic grounds—Judith Kaye, a famous judge on New York’s Court of Appeals and author of *W.W.W.*, was no political conservative—though it is harder to find political conservatives who embrace the priority of context over text.
9. Notice in *Trident* an emphasis on whether the parties are sophisticated and whether they were represented by lawyers. Should an interpretive regime be dependent on the status of the parties on these registers? Why or why not? How easy is it to know if someone is “sophisticated” or whether she has competent counsel? Should consumer contracts or contracts of adhesion have their own interpretive regimes? *See* Restatement (Second) of Contracts § 211 (developing an interpretive regime for “standardized agreements”; an approach that was not broadly adopted by courts); *C&J Fertilizer, Inc. v. Allied Mutual Insurance Company*, 227 N.W.2d 169 (Iowa 1975) (deciding that the “reasonable expectations” of the policyholder can prevail over the technical language of the insurance policy).
10. In 2006, in *Dore v. Arnold Worldwide, Inc.*, the California Supreme Court held that the defendant did not breach its contract with the plaintiff when it fired him without cause. Although the plaintiff wished to introduce evidence suggesting that he was not an at-will employee, the California Supreme Court affirmed the trial court decision that a trial

is not needed. Can this decision be reconciled with *Pacific Gas* or does it de facto embrace Judge Kozinski's call to change course? Is the California Supreme Court becoming more formalistic?

11. Are interpretive regimes mandatory rules or default rules? Perhaps a party could opt into New York or California law within a contract if parties were permitted to choose their applicable law (under choice of law rules that are outside the scope of this course). But could a party in New York enter a contract that instructs courts that they don't want *W.W.W.* to limit interpretation to the text of the agreement alone? Or might that be against the "public policy" of the state? See *Garden State Plaza Corp. v. S.S. Kresge Co.*, 189 A.2d 448 (N.J. Super. Ct. 1963) (holding as void against public policy a contract provision instructing that no "previous negotiations, arrangement, agreements and understandings" be used in the process of interpretation because "private agreement[s] mandating . . . performance of a judicial function" that requires "wearing judicial blinders" is "not the path to justice").

Is one's contract interpretive approach at least a strong predictor to one's approach to interpretation in general? Consider, for example, Professor Paul Freund's argument warning courts "not to read the provisions of the Constitution like a last will and testament, lest indeed they become one." Does it make sense to apply different interpretive rules depending on the nature of the legal text in question? Where does contract interpretation fit within this framework? Can you understand why one may hold a formalistic-textualist view in interpreting contracts but a less-textualist view when it comes to the interpretation of other legal text, such as the Constitution? Why or why not?

D. The Parol Evidence Rule

This section focuses on a specialized rule that, when properly understood (a rarity in courts, alas), is about the admission or exclusion of a species of extrinsic evidence. It is considered a substantive rule of contract law rather than a procedural or evidentiary rule, so might be misnamed for that reason among others. In the previous two sections, you learned about the genus of "extrinsic evidence," which could have included evidence of general context, courses of performance, courses of dealing, and usages of trade. Now we focus on a kind of extrinsic evidence that courts have grown especially concerned about admitting into evidence: parol evidence. Although the word "parol" is defined by "oral" evidence, referring to side agreements made orally prior to the final written agreement, in contemporary law "parol

evidence” can include prior oral or written agreements—or even negotiating history, whether oral or in writing (in memos or email or texts)—that precede what is a final written understanding between the parties.

Notice a few things about the scope of the parol evidence rule already: the rule deals with the impact of a final written agreement on the admissibility of evidence concerning prior or concurrent agreements and, more generally, the parties’ negotiation. It, therefore, only has application to cases *where there is final binding writing*. If your final deal is oral, the parol evidence rule is not applicable. If what you have as your contract is merely a document that is on the way to a final understanding but is not a final agreement, the rule should have no application. Sometimes parties will want to bring parol evidence to bear on the question of whether the agreement is actually a final one; nothing about the parol evidence rule disables the use of parol evidence to adjudicate the question of finality.

Similarly, the final written agreement needs to be in effect for the parol evidence rule to apply. Therefore, a side agreement that includes a condition for the effectiveness of the written agreement, is admissible. If, in October 2020, the parties conclude a final agreement for a cake celebrating Donald Trump for inauguration day but had a side agreement that the final agreement only comes into effect if Donald Trump is certified as the victor of the 2020 election in January 2021—the parol evidence rule won’t operate to exclude evidence of the condition precedent. Relatedly, if the cause of action is for fraud—or a party is claiming they were fraudulently induced into an agreement on the basis of parol evidence—or that there were severe defects in the formation of the alleged contract, such as lack of capacity, the parol evidence rule will not operate to exclude that evidence. Do you understand why the parol evidence rule cannot reasonably be used in those cases?

Finally, if what you are trying to admit into the court’s consideration is a side agreement that is itself a final agreement with its own independent consideration, then the rule has no application, either. If a party is selling a cake for \$50 in a final agreement but fails to note that the parties had already agreed that the buyer would also pay \$5 for the Tupperware in which it gets delivered, the parol evidence rule should not stop a party from trying to show evidence of the side deal for the Tupperware.

It should be apparent that the basic idea of the parol evidence rule rests on an intuition that it makes good sense to ask parties to put all their obligations in one place for ease of reference. It may even be a majoritarian kind of rule: most people probably see their final written agreements as containing the most important rights and obligations of their contracts. The

rules might therefore help most parties to distinguish between what was discussed but not agreed upon and what was actually agreed upon and is part of their agreement.

Applying the Parol Evidence Rule

We noted that the parol evidence rule deals with the possible exclusion (and admissibility) of the parties' agreements and interactions prior and at the contract formation. When it applies, we might say all such communications are "merged" into the final agreement. Contracts often contain what are called "merger" or "integration" or "entire agreement" clauses that announce, for example, "all the terms of this contract are here, in the contract, and nothing that came before is this contract or should be confused as such." There was such a clause in the contract at issue in *W.W.W.* above. But what are the implications of including such a clause? And, maybe more importantly, what about when there is no integration clause? Does the parol evidence rule insist on treating all contracts that don't have integration clauses as if they do?

Not quite. There are still some more technical terms to master: an agreement can be either *partially* or *completely* integrated. A *partially integrated* agreement is a final written agreement that cannot tolerate the use of parol evidence to *contradict* what is written in the agreement—but that wouldn't necessarily prevent a party from bringing parol evidence to *supplement* the agreement with an additional term. A *completely integrated* agreement, by contrast, of course cannot be contradicted by parol evidence but is also immune from the addition of supplementary terms through parol evidence. You can understand the logic of this division because not every final agreement is meant to cover every possible understanding that is part of the deal. Parties may have a final agreement and intend to have no negotiating history brought to bear to contradict the agreement but may in fact have discussed and agreed to a matter that just didn't make its way into the final writing at all. They may have agreed, for example, that a buyer was to pick up something from the seller's warehouse—but the buyer is instead demanding an overnight delivery, claiming that delivery is the default presumption and the seller should be excluded from bringing parol evidence of the "pick-up" agreement. A court seeing a written agreement whose scope doesn't cover pick-up or delivery terms could be justified in finding the agreement to be only partially integrated and admitting parol evidence of a side agreement for "pick-up."

But now we can see where some of the cleavages emerge in the jurisprudence of the parol evidence rule: just how can a court make these determinations about whether the agreement is wholly or partially integrated? In a way, this is why the parol evidence rule is also a rule about

interpretation: when can we interpret an agreement as a partially integrated writing and when are we justified in treating a writing as a completely integrated one? Can a court look at the parol evidence itself to decide whether the parol evidence can be brought to supplement the agreement? How carefully can a court consider the parol evidence to see if it contradicts the final writing or renders part of it ambiguous? And does the parol evidence rule just fall away once we say we are just using that evidence to *interpret* ambiguities rather than *contradict* or *supplement* the agreement? If everything turns on being able to differentiate the interpretive act of contradicting, supplementing, or explaining a term, is this a hopeless task?

There are a few general things we can say about these hard questions before we look at some cases. First, courts generally see it as their role to make decisions as a matter of law about finality and the kind of integration that there is. So, although in the jurisprudence of the parol evidence rule there is a fair bit of talk about confusing the jury if the court agrees to admit the evidence, at the early stages of a litigation when a court is making legal determinations about integration, it could theoretically be able to peek at the parol evidence to help it make its legal ruling on those threshold questions. Not all courts will be willing to do that on integration, though most will on finality.

Second, many courts, especially the more formalistic ones, are primed to be skeptical about claims of side deals outside the final writing: indeed, although parties may want to highlight parol evidence because it felt to them that the representations made during negotiations are hugely relevant to why they got into the deal in the first place (remember *W.W.W.?*), the parol evidence rule usually operates to favor the final written agreement.

Third, it is important to understand that once we cross over into the realm of pure “interpretation” (not that it will always be clear when a party is trying to add a term, contradict a term, or interpret a term), we are outside the scope of the exclusionary parol evidence rule, formally speaking. In other words, the parol evidence rule does not purport to exclude evidence presented to clarify the meaning of an ambiguous term in the writing. Courts are mealy-mouthed here, in part because courts with an exclusionary attitude to extrinsic evidence (those are the more formalistic courts such as the New Court of Appeals) generally aren’t all of a sudden inclusionary when the formalities of the parol evidence rule stop applying—and in part because the more inclusionary courts (such as the California Supreme Court) tend to harmonize their approaches to extrinsic evidence, whether parol or otherwise, as well. But it isn’t really contested that once we are interpreting an agreement, the interpretation regime (such as we learned above) takes over from more specialized rules about parol evidence.

The Two Main Approaches

There are two general approaches to the most central issue of integration. They are summarized in John D. Calamari & Joseph M. Perillo, *A Plea for a Uniform Parol Evidence Rule and Principles of Contract Interpretation*, 42 INDIANA L.J. 333 (1967), which we highly recommend to those interested in gaining deeper understanding on this topic. Calamari & Perillo call them the “Willistonian” and the “Corbinite” approaches. In some respects, these stylized positions map onto the contract scholars Samuel Williston and Arthur Corbin. The first was the reporter and is often identified with the First Restatement of Contracts, while the latter was the reporter and recognized as one of the main scholars behind the Second Restatement of Contracts. The Willistonian position was more or less adopted in New York and the Corbinite position was more or less adopted in California.

For the Willistonians, the parol evidence rule is about document protection at its core. The plain meaning of the document ought to control on the question of integration. If there is an integration clause, all the better: it will be followed. If there isn’t, the court should make a determination within the four corners of the document about what kind of integration it is looking at. If the side agreement would, however, “naturally” be made outside the agreement, a court may consider supplementing the agreement with such a term—so long as “ordinarily” the final agreement wouldn’t already be expected to cover that term. Willistonians would be loath to look at the parol evidence itself to make a determination about integration unless there was an ambiguity within the agreement.

By contrast, Corbinites would treat the question of integration as a question of intent, as any other. All relevant and credible evidence on the issue can be reviewed to make a determination—even parol evidence and even in a case of a contract with an integration clause. Does this, then, eviscerate the whole point of the parol evidence rule? Maybe. But maybe not: perhaps judges can still prevent bad parol evidence from going to the jury and can give them a better sense of what kind of integration, partial or complete, they are really dealing with.

Before we move to some cases, understand what is at stake in what may feel already like a debate well in the weeds of technical terminology. On the one hand, there is nothing wrong with channeling parties to get their written agreements in one place rather than on some emails and text chains. We also want to help companies control their agency problems and not have home offices become bound by representations their self-motivated officers working on commissions make to promisees who need to be conformed to a standardized agreement. Furthermore, we want to simplify the ex-post adjudication process. But a harsh parol evidence does risk giving even more power to those who control agreements in the first place (especially

in consumer transactions) and risks not giving people their real deals in favor of a fictional paper deal. It might also burden the ex-ante negotiation process. Do you see why?

Let's look at some exemplary cases in the common law before moving on to the UCC's approach to parol evidence.

Mitchill v. Lath

160 N.E. 646 (N.Y. Court of Appeals 1928)

ANDREWS, Judge

In the fall of 1923 the Laths owned a farm. This they wished to sell. Across the road, on land belonging to Lieutenant Governor Lunn, they had an icehouse which they might remove. Mrs. Mitchill looked over the land with a view to its purchase. She found the icehouse objectionable. Thereupon 'the defendants orally promised and agreed, for and in consideration of the purchase of their farm by the plaintiff, to remove the said icehouse in the spring of 1924.' Relying upon this promise, she made a written contract to buy the property for \$8,400, for cash and mortgage and containing various provisions usual in such papers. Later receiving a deed, she entered into possession, and has spent considerable sums in improving the property for use as a summer residence. The defendants have not fulfilled their promise as to the icehouse, and do not intend to do so. We are not dealing, however, with their moral delinquencies. The question before us is whether their oral agreement may be enforced in a court of equity.

This requires a discussion of the parol evidence rule—a rule of law which defines the limits of the contract to be construed. It is more than a rule of evidence, and oral testimony, even if admitted, will not control the written contract, unless admitted without objection. It applies, however, to attempts to modify such a contract by parol. It does not affect a parol collateral contract distinct from and independent of the written agreement. It is, at times, troublesome to draw the line. Williston, in his work on Contracts points out the difficulty. 'Two entirely distinct contracts,' he says, 'each for a separate consideration, may be made at the same time, and will be distinct legally. Where, however, one agreement is entered into wholly or partly in consideration of the simultaneous agreement to enter into another, the transactions are necessarily bound together. Then if one of the agreements is oral and the other in writing, the problem arises whether the bond is sufficiently close to prevent proof of the oral agreement.' That is the situation here. It is claimed that the defendants are called upon to do more than is required by their written contract in connection with the sale as to which it deals.

The principal may be clear, but it can be given effect by no mechanical rule. As so often happens it is a matter of degree, for, as Prof. Williston also says, where a contract contains several promises on each side it is not difficult to put any one of them in the form of a collateral agreement. If this were enough, written contracts might always be modified by parol. Not form, but substance, is the test.

In applying this test, the policy of our courts is to be considered. We have believed that the purpose behind the rule was a wise one, not easily to be abandoned. Notwithstanding injustice here and there, on the whole it works for good. . . . New York has been less open to arguments that would modify this particular rule, than some jurisdictions elsewhere. . . .

Under our decisions before such an oral agreement as the present is received to vary the written contract, at least three conditions must exist: (1) The agreement must in form be a collateral one; (2) it must not contradict express or implied provisions of the written contract; (3) it must be one that parties would not ordinarily be expected to embody in the writing, or, put in another way, an inspection of the written contract, read in the light of surrounding circumstances, must not indicate that the writing appears 'to contain the engagements of the parties, and to define the object and measure the extent of such engagement.' Or, again, it must not be so clearly connected with the principal transaction as to be part and parcel of it.

The respondent does not satisfy the third of these requirements. It may be, not the second. We have a written contract for the purchase and sale of land. The buyer is to pay \$8,400 in the way described. She is also to pay her portion of any rents, interest on mortgages, insurance premiums, and water meter charges. She may have a survey made of the premises. On their part, the sellers are to give a full covenant deed of the premises as described, or as they may be described by the surveyor, if the survey is had, executed, and acknowledged at their own expense; they sell the personal property on the farm and represent they own it; they agree that all amounts paid them on the contract and the expense of examining the title shall be a lien on the property; they assume the risk of loss or damage by fire until the deed is delivered; and they agree to pay the broker his commissions. Are they to do more? Or is such a claim inconsistent with these precise provisions? It could not be shown that the plaintiff was to pay \$500 additional. Is it also implied that the defendants are not to do anything unexpressed in the writing?

That we need not decide. At least, however, an inspection of this contract shows a full and complete agreement, setting forth in detail the obligations of each party. On reading it, one would conclude that the reciprocal obligations of the parties were fully detailed. Nor would

his opinion alter if he knew the surrounding circumstances. The presence of the icehouse, even the knowledge that Mrs. Mitchill thought it objectionable, would not lead to the belief that a separate agreement existed with regard to it. Were such an agreement made it would seem most natural that the inquirer should find it in the contract. Collateral in form it is found to be, but it is closely related to the subject dealt with in the written agreement—so closely that we hold it may not be proved....

LEHMAN, J. (dissenting).

I accept the general rule as formulated by Judge ANDREWS. I differ with him only as to its application to the facts shown in the record. . . .

I think we agree that the first condition that the agreement ‘must in form be a collateral one’ is met by the evidence. I concede that this condition is met in most cases where the courts have nevertheless excluded evidence of the collateral oral agreement. The difficulty here, as in most cases, arises in connection with the two other conditions.

The second condition is that the ‘parol agreement must not contradict express or implied provisions of the written contract.’ Judge ANDREWS voices doubt whether this condition is satisfied. The written contract has been carried out. The purchase price has been paid; conveyance has been made; title has passed in accordance with the terms of the written contract. The mutual obligations expressed in the written contract are left unchanged by the alleged oral contract. When performance was required of the written contract, the obligations of the parties were measured solely by its terms. By the oral agreement the plaintiff seeks to hold the defendants to other obligations to be performed by them thereafter upon land which was not conveyed to the plaintiff.

The assertion of such further obligation is not inconsistent with the written contract, unless the written contract contains a provision, express or implied, that the defendants are not to do anything not expressed in the writing. Concededly there is no such express provision in the contract, and such a provision may be implied, if at all, only if the asserted additional obligation is ‘so clearly connected with the principal transaction as to be part and parcel of it,’ and is not ‘one that the parties would not ordinarily be expected to embody in the writing.’ The hypothesis so formulated for a conclusion that the asserted additional obligation is inconsistent with an implied term of the contract is that the alleged oral agreement does not comply with the third condition as formulated by Judge ANDREWS. In this case, therefore, the problem reduces itself to the one question whether or not the oral agreement meets the third condition. . . .

I have conceded that upon inspection the contract is complete. 'It appears to contain the engagements of the parties, and to define the object and measure the extent of such engagement;' it constitutes the contract between them, and is presumed to contain the whole of that contract. That engagement was on the one side to convey land; on the other to pay the price. The plaintiff asserts further agreement based on the same consideration to be performed by the defendants after the conveyance was complete, and directly affecting only other land. It is true, as Judge ANDREWS points out, that 'the presence of the icehouse, even the knowledge that Mrs. Mitchill thought it objectionable, would not lead to the belief that a separate agreement existed with regard to it'; but the question we must decide is whether or not, assuming an agreement was made for the removal of an unsightly icehouse from one parcel of land as an inducement for the purchase of another parcel, the parties would ordinarily or naturally be expected to embody the agreement for the removal of the icehouse from one parcel in the written agreement to convey the other parcel. Exclusion of proof of the oral agreement on the ground that it varies the contract embodied in the writing may be based only upon a finding or presumption that the written contract was intended to cover the oral negotiations for the removal of the icehouse which lead up to the contract of purchase and sale. To determine what the writing was intended to cover, 'the document alone will not suffice. What it was intended to cover cannot be known till we know what there was to cover. The question being whether certain subjects of negotiation were intended to be covered, we must compare the writing and the negotiations before we can determine whether they were in fact covered.' The subject-matter of the written contract was the conveyance of land. The contract was so complete on its face that the conclusion is inevitable that the parties intended to embody in the writing all the negotiations covering at least the conveyance. The promise by the defendants to remove the icehouse from other land was not connected with their obligation to convey except that one agreement would not have been made unless the other was also made. The plaintiff's assertion of a parol agreement by the defendants to remove the icehouse was completely established by the great weight of evidence. It must prevail unless that agreement was part of the agreement to convey and the entire agreement was embodied in the writing.

The fact that in this case the parol agreement is established by the overwhelming weight of evidence is, of course, not a factor which may be considered in determining the competency or legal effect of the evidence. Hardship in the particular case would not justify the court in disregarding or emasculating the general rule. It merely accentuates the outlines of our problem. The assumption that the parol agreement was made is no longer obscured by any doubts.

The problem, then, is clearly whether the parties are presumed to have intended to render that parol agreement legally ineffective and nonexistent by failure to embody it in the writing. Though we are driven to say that nothing in the written contract which fixed the terms and conditions of the stipulated conveyance suggests the existence of any further parol agreement, an inspection of the contract, though it is complete on its face in regard to the subject of the conveyance, does not, I think, show that it was intended to embody negotiations or agreements, if any, in regard to a matter so loosely bound to the conveyance as the removal of an icehouse from land not conveyed.

The rule of integration undoubtedly frequently prevents the assertion of fraudulent claims. Parties who take the precaution of embodying their oral agreements in a writing should be protected against the assertion that other terms of the same agreement were not integrated in the writing. The limits of the integration are determined by the writing, read in the light of the surrounding circumstances. A written contract, however complete, yet covers only a limited field. I do not think that in the written contract for the conveyance of land here under consideration we can find an intention to cover a field so broad as to include prior agreements, if any such were made, to do other acts on other property after the stipulated conveyance was made.

In each case where such a problem is presented, varying factors enter into its solution. Citation of authority in this or other jurisdictions is useless, at least without minute analysis of the facts. The analysis I have made of the decisions in this state leads me to the view that the decision of the courts below is in accordance with our own authorities and should be affirmed.

CARDOZO, C. J., and POUND, KELLOGG and O'BRIEN, JJ., concur with ANDREWS, J. LEHMAN, J., dissents in opinion in which CRANE, J., concurs.

Notes and Questions

1. If you already had the chance to encounter Judge Cardozo and his jurisprudence before, were you surprised to see him signing onto the majority opinion in *Mitchill*?
2. Are you troubled by the fact that no one seems to deny that the Laths promised Ms. Mitchill that they would remove the icehouse, yet the majority excludes evidence of this deal despite its alleged importance to Ms. Mitchill? Is this an example of a court denigrating something it thought was “merely” a feminine aesthetic concern? Can it

even be argued that the contract, as the court enforces it—without the promise to remove the icehouse—corresponds to the parties’ intent?

3. Consider a different type of possible justification for the majority view. A few years before its decision in *Mitchill*, the New York Court of Appeals decided, over a strongly worded dissent in *Sun Printing & Publishing Association v. Remington Paper & Power Company*, that parties failed to create a year-long agreement because their written agreement was not complete enough. You might encounter that case in a different part of this course. In a lecture given shortly thereafter, Benjamin Cardozo, the legendary Chief Judge of the Court, who authored *Sun Printing* (and later joined the majority in *Mitchill*), addressed the possible perceived injustice in the Court’s formalistic approach:

The court subordinated the equity of a particular situation to the overmastering need of certainty in the transactions of commercial life . . . In this department of activity, the current axiology still places stability and certainty in the forefront of the virtues.

BENJAMIN CARDOZO, *GROWTH OF THE LAW* 110-111 (1924). Do you think this reasoning can apply to *Mitchill* as well? Is this a convincing argument?

4. We explained that an integrated written agreement can be partly integrated or completely integrated. That is the approach and the terminology that the Restatement adopted as well. *See* Restatement (Second) of Contracts §§ 210, 213. The court in *Mitchill* does not explicitly use those terms, but both the majority and the dissent seem to imply that the document was completely integrated. Notice, however, that even if an agreement is completely integrated it only “discharges prior agreement *to the extent that they are within its scope*,” *id.*, § 213(2) (emphasis added). That seems to be the main source of disagreement here.
5. If the decision comes down to whether “the parties would ordinarily or naturally be expected to embody the agreement for the removal of the icehouse from one parcel in the written agreement to convey the other parcel,” doesn’t that sound like a factual question or at least a question about what reasonable parties would do? If so, why do judges and not the jury get to apply the parol evidence rule?
6. Are you convinced this is really a Willistonian opinion—putting to one side that Williston is cited all over it?

7. Test your knowledge of the New York approach to parol evidence now that you have both *W.W.W.* and *Mitchill* under your belt. Could the court in *Frigaliment* look at parol evidence of the meaning intended by the parties on “what is chicken”? Why or why not?

Now let’s look at a more Corbinite approach. As you’ll see, the specification of the rules themselves aren’t wildly different but their applications come from a very different ethos that is more permissive and less concerned with the sanctity of writings. As with *Mitchill*, an excerpt of the dissent is included below to highlight that even in the jurisdictions with differentiated versions of the parol evidence rule, judges don’t easily agree on how to apply the “rule.”

Masterson v. Sine

436 P.2d 561 (Supreme Court of California 1968)

TRAYNOR, Chief Justice.

Dallas Masterson and his wife Rebecca owned a ranch as tenants in common. On February 25, 1958, they conveyed it to Medora and Lu Sine by a grant deed ‘Reserving unto the Grantors herein an option to purchase the above described property on or before February 25, 1968’ for the ‘same consideration as being paid heretofore plus their depreciation value of any improvements. Grantees may add to the property from and after two and a half years from this date.’ Medora is Dallas’ sister and Lu’s wife.

Since the conveyance Dallas has been adjudged bankrupt. His trustee in bankruptcy and Rebecca brought this declaratory relief action to establish their right to enforce the option.

The case was tried without a jury. The [trial] court . . . determined that the parol evidence rule precluded admission of extrinsic evidence offered by defendants to show that the parties wanted the property kept in the Masterson family and that the option was therefore personal to the grantors and could not be exercised by the trustee in bankruptcy. . . .

Defendants appeal. . . . The trial court erred . . . in excluding the [parol] evidence that the option was personal to the grantors and therefore nonassignable.

When the parties to a written contract have agreed to it as an ‘integration’—a complete and final embodiment of the terms of an agreement—parol evidence cannot be used to add to or vary its terms. See 3 Corbin, Contracts (1960) s 573, p. 357. When only part of the agreement

is integrated, the same rule applies to that part, but parol evidence may be used to prove elements of the agreement not reduced to writing. The crucial issue in determining whether there has been an integration is whether the parties intended their writing to serve as the exclusive embodiment of their agreement. The instrument itself may help to resolve that issue. It may state, for example, that ‘there are no previous understandings or agreements not contained in the writing,’ and thus express the parties’ ‘intention to nullify antecedent understandings or agreements.’ (See 3 Corbin, *Contracts* (1960) s 578, p. 411.) Any such collateral agreement itself must be examined, however, to determine whether the parties intended the subjects of negotiation it deals with to be included in, excluded from, or otherwise affected by the writing. Circumstances at the time of the writing may also aid in the determination of such integration. (See 3 Corbin, *Contracts* (1960) ss 582—584).

California cases have stated that whether there was an integration is to be determined solely from the face of the instrument, and that the question for the court is whether it ‘appears to be a complete agreement.’ Neither of these strict formulations of the rule, however, has been consistently applied. The requirement that the writing must appear incomplete on its face has been repudiated in many cases where parol evidence was admitted ‘to prove the existence of a separate oral agreement as to any matter on which the document is silent and which is not inconsistent with its terms’—even though the instrument appeared to state a complete agreement. Even under the rule that the writing alone is to be consulted, it was found necessary to examine the alleged collateral agreement before concluding that proof of it was precluded by the writing alone. (See 3 Corbin, *Contracts* (1960) s 582, pp. 444—446.) It is therefore evident that ‘The conception of a writing as wholly and intrinsically self-determinative of the parties’ intent to make it a sole memorial of one or seven or twenty-seven subjects of negotiation is an impossible one.’

In formulating the rule governing parol evidence, several policies must be accommodated. One policy is based on the assumption that written evidence is more accurate than human memory. This policy, however, can be adequately served by excluding parol evidence of agreements that directly contradict the writing. Another policy is based on the fear that fraud or unintentional invention by witnesses interested in the outcome of the litigation will mislead the finder of facts. (*Mitchill v. Lath* (1928) (dissenting opinion by Lehman, J.). McCormick has suggested that the party urging the spoken as against the written word is most often the economic underdog, threatened by severe hardship if the writing is enforced. In his view the parol evidence rule arose to allow the court to control the tendency of the jury to find through sympathy and without a dispassionate assessment of the probability of fraud or faulty memory that the parties made an oral agreement collateral to the written contract, or that preliminary

tentative agreements were not abandoned when omitted from the writing. He recognizes, however, that if this theory were adopted in disregard of all other considerations, it would lead to the exclusion of testimony concerning oral agreements whenever there is a writing and thereby often defeat the true intent of the parties.

Evidence of oral collateral agreements should be excluded only when the fact finder is likely to be misled. The rule must therefore be based on the credibility of the evidence. One such standard, adopted by section 240(1)(b) of the Restatement of Contracts, permits proof of a collateral agreement if it 'is such an agreement as might naturally be made as a separate agreement by parties situated as were the parties to the written contract.' The draftsmen of the Uniform Commercial Code would exclude the evidence in still fewer instances: 'If the additional terms are such that, if agreed upon, they would certainly have been included in the document in the view of the court, then evidence of their alleged making must be kept from the trier of fact.' (Com. 3, s 2—202.)¹

The option clause in the deed in the present case does not explicitly provide that it contains the complete agreement, and the deed is silent on the question of assignability. Moreover, the difficulty of accommodating the formalized structure of a deed to the insertion of collateral agreements makes it less likely that all the terms of such an agreement were included. The statement of the reservation of the option might well have been placed in the recorded deed solely to preserve the grantors' rights against any possible future purchasers and this function could well be served without any mention of the parties' agreement that the option was personal. There is nothing in the record to indicate that the parties to this family transaction, through experience in land transactions or otherwise, had any warning of the disadvantages of failing to put the whole agreement in the deed. This case is one, therefore, in which it can be said that a collateral agreement such as that alleged 'might naturally be made as a separate agreement.' A fortiori, the case is not one in which the parties 'would certainly' have included the collateral agreement in the deed.

¹ Corbin suggests that, even in situations where the court concludes that it would not have been natural for the parties to make the alleged collateral oral agreement, parol evidence of such an agreement should nevertheless be permitted if the court is convinced that the unnatural actually happened in the case being adjudicated. This suggestion may be based on a belief that judges are not likely to be misled by their sympathies. If the court believes that the parties intended a collateral agreement to be effective, there is no reason to keep the evidence from the jury.

It is contended, however, that an option agreement is ordinarily presumed to be assignable if it contains no provisions forbidding its transfer or indicating that its performance involves elements personal to the parties. The fact that there is a written memorandum, however, does not necessarily preclude parol evidence rebutting a term that the law would otherwise presume. In *American Industrial Sales Corp. v. Airscope, Inc.*, we held it proper to admit parol evidence of a contemporaneous collateral agreement as to the place of payment of a note, even though it contradicted the presumption that a note, silent as to the place of payment, is payable where the creditor resides. . . .

In the present case defendants offered evidence that the parties agreed that the option was not assignable in order to keep the property in the Masterson family. The trial court erred in excluding that evidence. The judgment is reversed.

BURKE, Justice.

I dissent. The majority opinion:

- (1) Undermines the parol evidence rule as we have known it in this state since at least 1872 by declaring that parol evidence should have been admitted by the trial court to show that a written option, absolute and unrestricted in form, was intended to be limited and nonassignable;
- (2) Renders suspect instruments of conveyance absolute on their face;
- (3) Materially lessens the reliance which may be placed upon written instruments affecting the title to real estate; and
- (4) Opens the door, albeit unintentionally to a new technique for the defrauding of creditors.

The opinion permits defendants to establish by parol testimony that their grant to their brother (and brother-in-law) of a written option, absolute in terms, was nevertheless agreed to be nonassignable by the grantee (now a bankrupt), and that therefore the right to exercise it did not pass, by operation of the bankruptcy laws, to the trustee for the benefit of the grantee's creditors.

And how was this to be shown? By the proffered testimony of the bankrupt optionee himself! Thereby one of his assets (the option to purchase defendants' California ranch) would be withheld from the trustee in bankruptcy and from the bankrupt's creditors. Understandably the trial court, as required by the parol evidence rule, did not allow the bankrupt by parol to

so contradict the unqualified language of the written option. . . . The right of an optionee to transfer his option to purchase property is accordingly one of the basic rights which accompanies the option unless limited under the language of the option itself. To allow an optionor to resort to parol evidence to support his assertion that the written option is not transferable is to authorize him to limit the option by attempting to restrict and reclaim rights with which he has already parted. A clearer violation of two substantive and basic rules of law—the parol evidence rule and the right of free transferability of property—would be difficult to conceive. . . .

Notes and Questions

1. Can you see how Chief Justice Traynor, who is widely considered one of the most prominent state court judges of his century, is influenced by a Corbinite approach here?
2. Is the only possible explanation of the differences between the results in *Mitchill* and *Masterson* the interpretative philosophy of the courts? What other facts, if any, can distinguish those two cases?
3. Does it seem very likely to you that this parol agreement was made prior to the final written expression? On the other hand, the majority mentions that one of the justifications for excluding parol evidence is the fear of fraud. Is that concern relevant in this case?
4. How central is the McCormick thesis to Traynor's refashioning of the California parol evidence rule in *Masterson*, that "the party urging the spoken as against the written word is most often the economic underdog, threatened by severe hardship if the writing is enforced"? If the empirical evidence points in another direction, should Traynor shift course? Is the parol evidence rule a good place to engage in redistributive politics?
5. Do you see a circularity problem in Traynor's position: A parol agreement is excluded if there is a complete integration but whether it is an integration depends on the credibility of the parol evidence. Do you see a way this might not be a vicious circle?
6. The dissent suggests that relaxing the parol evidence rule might harm third parties. Do you understand why and when that might happen? Should that affect how third parties are likely to behave when encountering, and relying on, an agreement that has a New York choice of law versus one that has a California one?

The majority opinion in *Masterson* points to what it takes to be an even more liberal rule in the UCC (pointing to comment 3 to § 2-202): parol evidence is inadmissible only if the parol agreement would certainly have been included in the final agreement. Although *Masterson* claims to be coming shy of being as liberal as UCC's articulation, let's look at § 2-202 again (now with more parts specifically about parol evidence rather than just course of performance, course of dealing and usage of trade which we have already seen), along with a case applying it.

§ 2-202. Final Written Expression: Parol or Extrinsic Evidence.

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

- (a) by course of dealing or usage of trade or by course of performance; and
- (b) 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.

Binks Manufacturing Co. v. National Presto Industries, Inc.

709 F.2d 1109 (7th Cir. 1983)

COFFEY, Judge.

This appeal involves a contractual dispute concerning the manufacture and sale of an "industrial spray finishing and baking system." Binks Manufacturing Company, the System's manufacturer, brought an action in federal district court to collect the purchase price of the System. Presto Manufacturing Company, counterclaimed alleging damages resulting from defective design and manufacture of the System as well as late delivery. The jury returned verdicts in favor of Binks on its purchase price claim and against Presto on its counterclaims. We affirm.

I.

Presto is engaged in the manufacture and sale of electrical appliances, including hamburger cookers. Binks Manufacturing Company is a leading manufacturer of industrial spray finishing equipment. In 1975, Presto management decided to increase its production capacity of electric hamburger cookers and as part of its expansion plan, determined to purchase an automatic system designed to coat aluminum castings (the principal components of hamburger cookers) with a non-stick “teflon-like” coating for installation at its Alamogordo, New Mexico plant. Presto entered into negotiations with Binks Manufacturing Company for the design and manufacture of the system.

The negotiations between Binks and Presto continued from October 1975 through March 1976, resulting in a contract with Binks agreeing to manufacture “a custom designed, custom built automatic spray application and oven curing system intended to apply coatings to various Presto products” (hereinafter the “System”). The System was to consist of one continuous conveyor 858 feet long, designed to carry an aluminum casting through a six-step manufacturing process: (1) a booth in which the castings would be sprayed with a primer; (2) an oven where the primer would be baked on to the aluminum castings; (3) a cooling area; (4) a booth where the castings would be sprayed with a non-stick coating; (5) three progressively hotter ovens in which the nonstick coating would be baked on to the aluminum castings over the primer; and (6) a final cooling area. ...

The contract also provided that shipment of the System to Presto’s plant “will not be made later than June 2, 1976” and further states that “[t]ime is of the essence” On May 26, 1976, Binks informed Presto that shipment of the System could not be completed until mid-June of 1976, approximately two weeks later than the agreed upon delivery date. In reality, shipment of the System to Presto’s Alamogordo, New Mexico plant was not accomplished until July 19, 1976. Binks’ late delivery of the System was due to their inability to obtain timely delivery from the oven subcontractor, Radiant Products. Radiant, in turn, attributed their late shipment to an unforeseen shutdown of a Radiant supplier’s plant (U.S. Gypsum) and an unforeseen injury to a key Radiant employee.

Binks offered to supervise installation of the System, but Presto chose not to accept the offer and hired their own local independent contractors to install the System. According to Binks, Presto’s independent contractors committed installation errors of major proportions, including a failure to properly align and anchor the conveyor equipment. Binks further contends that Presto insisted upon initially operating the System at maximum capacity, thereby ignoring Binks’ advice that the System be brought up to full capacity only gradually.

After installation of the System had been completed, Presto personnel made several unsuccessful attempts to operate the System's conveyor. In the ensuing weeks representatives of Presto, Binks and Radiant made other attempts to operate the System, but experienced a myriad of problems. Binks contends that Presto's independent contractors failed to properly synchronize the electric motors used to run the conveyor causing the conveyor to run sporadically and jam. These problems in conveyor synchronization continued for some two months causing the System to operate at less than half capacity.

Binks and Presto disagree as to the underlying cause of the System's faulty performance. Presto alleges that the System was defectively manufactured in that the conveyor, contrary to the contract specifications, was totally enclosed in the System's ovens, causing the conveyor components to overheat, contributing to the twisting, bending and eventually breakage of the conveyor chain.

Binks, on the other hand, contends Presto: (1) improperly installed the System; (2) inadequately lubricated the conveyor; (3) operated the System's oven at excessive temperatures; (4) ignored Binks' advice in initially operating the System at maximum capacity; and (5) ran defective castings through the System, resulting in pieces breaking off the castings and jamming the conveyor.

Binks also asserts that Presto abused the System by "double loading" the castings used to make upper components of the hamburger cookers, thereby exceeding the System's maximum capacity set forth in the contract. According to Binks, "double loading" the System resulted in twice as many upper burger castings being loaded into the System per hour as specified in the contract (2,250 "upper double burger" castings per hour instead of the 1,125 castings per hour outlined in the contract and 4,500 "upper square burger" castings per hour rather than 2,250 castings per hour set forth in the contract). ...

Binks and Presto made several unsuccessful attempts to reach a negotiated settlement and failing to achieve this, on November 4, 1977, Binks filed a complaint seeking recovery under the contract for the balance of the purchase price. Presto answered by filing a \$9.5 million counterclaim against Binks alleging late delivery of the System, breach of contractual warranties, breach of implied warranties, negligence and misrepresentation in connection with the design, manufacture and sale of the spraying and baking system. ...

The case came to trial on March 1, 1982, and after the four-week jury trial, judgment was entered in favor of Binks on its claim for the balance of the purchase price

On appeal, Presto contends that the district court erred:

1. In granting Binks’ pre-trial motion in limine, precluding Presto from introducing parol and extrinsic evidence to attempt to show that the parties intended to define the maximum capacity of the System in terms of pounds of castings per hour, rather than the number of castings per hour. . . .

II.

THE MOTION IN LIMINE CONCERNING THE ISSUE OF MAXIMUM CAPACITY

Presto’s counterclaim against Binks alleged that the System designed and manufactured by Binks was defective, resulting in repeated breakdowns and loss of production. Binks answered that the System’s breakdowns were not a result of defective design or manufacture, but rather were caused by Presto’s abuse of the System, particularly Presto’s practice of “double loading” the System.

Therefore, to establish this “double loading” theory at trial, it became necessary to determine the System’s “maximum capacity” as defined in the parties’ contract. The parties agree that the following provision of the contract sets forth the System’s maximum capacity:

[DESCRIPTION

In accordance with your request, we are pleased to submit for your consideration, a revised quotation covering:]

One Item of Equipment designed to coat any one of the following parts on one and/or both sides in quantities, as listed at the conveyor rate of 25 fpm with either 16 or 18 inch spindle spacing:

#60-001	Upper Double Burger at (13 oz.)	1,125 pcs./hr.
#60-002	Lower Double Burger at (24 oz.)	1,125 pcs./hr.
#60-003	Upper Square Burger (9.5 oz.)	2,250 pcs./hr.
#60-004	Lower Square Burger (12 oz.)	2,250 pcs./hr.
#60-121	Upper Round Burger (7 oz.)	2,250 pcs./hr.
#60-120	Lower Round Burger (5 oz.)	2,250 pcs./hr.
#28-006	Fry Pan at 3.8#—Quantities as later established.	

The maximum capacity of the system is limited to the above parts or parts of similar size and cross section with a maximum loading of 4,500 pounds per hour and 4,500 #/hr. of work holders, which would pass through each oven.

Based on the foregoing contractual language, Binks takes the position that the “maximum capacity” of the System for the castings specified in the contract is defined in terms of the *number* of castings that the System can handle per hour consistent with the design of the machine. Presto, however, contends that extrinsic evidence concerning negotiation and performance of the contract demonstrates that the parties intended the maximum capacity of the System to be defined in terms of *pounds* of castings run through the System per hour; i.e., 4,500 pounds of castings per hour. Presto further argues, and Binks concedes, that Presto never loaded the System with more than 4,500 pounds of castings per hour.

Presto, in support of its contention that the parties intended the System’s maximum capacity to be defined in *pounds* per hour, sought to introduce extrinsic evidence pertaining to the negotiation and performance of the contract.⁶ On February 25, 1976, four days before trial, Binks presented a motion in limine seeking an order precluding Presto from presenting extrinsic evidence to show that the parties intended to define the maximum capacity of the System in terms of pounds per hour rather than number of castings per hour. After hearing arguments, the court ruled in favor of Binks on the motion in limine and stated:

I conclude that so far as the six identified parts are concerned, the specified maximums of the system are those numbers appearing opposite each of the items [in the contract provision quoted above] and not the number of items which would aggregate 4,500 pounds.

Presto contends the court committed reversible error in ruling that Presto could not introduce extrinsic evidence to show that the parties intended to define the System’s maximum capacity in pounds per hour.

In evaluating Presto’s challenge to the district court’s ruling, we must bear in mind that our role as an appellate court is not to consider a case *de novo*. Rather, our role in reviewing the

⁶ This [] evidence included inter alia: (1) a quotation submitted by Binks several days prior to formation of the contract stating “approximately 4,500 pounds of aluminum work pieces ... will pass through each oven per hour;” (2) a March 9, 1976 letter from Binks’ project engineer to Presto reciting “The System capacity increased from 1500 to 4500 # /Hr.,” and (3) that Binks participated in designing the work holders in which castings were placed, and allowed for “double loading” of castings.

district court's ruling on the motion in limine is limited as "decisions regarding the admission and exclusion of evidence are peculiarly within the competence of the district court and will not be reversed on appeal unless they constitute a clear abuse of discretion." . . .

Guided by these principles, we turn to the issue of whether the court abused its discretion by precluding Presto from introducing extrinsic evidence to establish that the parties intended the System's maximum capacity for "Upper Double Burger" and "Upper Square Burger" castings to be defined in pounds per hour, rather than number of castings per hour. The admissibility of extrinsic evidence to interpret the contract in this case is governed by Ill.Rev.Stat. ch. 26, section 2-202. . . .

[U]nder UCC section 2-202, evidence of a prior agreement or a contemporaneous oral agreement must be excluded if (1) the writing (here the contract between the parties) was intended as the final expression of the parties' agreement with respect to the maximum capacity term; and (2) the proffered evidence contradicts or is inconsistent with the terms of the written contract. It is evident from the record that both Binks and Presto agree that their written contract was intended to be the final expression of their agreement; therefore, the crucial question is whether the interpretation urged by Presto (i.e., that the parties intended the System's maximum capacity for "Upper Square Burger" and "Upper Double Burger" castings to be a function of pounds of castings per hour) contradicts or is inconsistent with the terms of the written contract.

Although the Uniform Commercial Code itself fails to delineate or set forth when extrinsic evidence contradicts or is inconsistent with written terms of a contract, this court recently defined "inconsistency" for the purpose of UCC section 2-202 as "the absence of reasonable harmony in terms of the language and respective obligations of the parties." Applying this definition of "inconsistency" to this case, it is clear that if the court were to allow the admission of extrinsic evidence tending to show that the maximum capacity of the System for "Upper Square Burger" and "Upper Double Burger" castings was defined in terms of pounds per hour it would necessarily lead to an "absence of reasonable harmony" between the terms of the written contract and the proffered extrinsic evidence of the parties' purported intent. Presto's theory that the System's maximum capacity for the upper burger castings was defined as 4,500 pounds of such castings per hour would render almost meaningless the express language of the written contract which, after reciting a specified number of each particular casting, states "the maximum capacity of the System is limited to the above parts" On the other hand, the district court's well reasoned interpretation of the written contract gave meaning to each and every provision of the contract; for each of the six castings listed, the maximum capacity of

the System was defined in number of parts per hour, while for other unspecified castings which Presto might decide to run through the System in the future, the maximum capacity was defined in pounds of castings per hour. Thus, the court's decision to exclude the extrinsic evidence of the parties intent is amply supported by the basic principles of contract interpretation that a written contract should be given a construction that "harmonizes all the various parts" of the contract so that no provision is "conflicting with, or repugnant to, or neutralizing of any other."

Furthermore, the district court's decision to preclude Presto from introducing [parol or] extrinsic evidence regarding the maximum capacity issue pays credence to the policy underlying the parol evidence rule as set forth in UCC section 2-202. This court . . . stated: "The parol evidence rule ... is a rule of substantive law. Evidence is excluded not because it is not credible or not relevant but because of a policy favoring the reliability of written representations of the terms of a contract."

This policy of upholding the integrity of written contracts and favoring written terms over extrinsic evidence is particularly relevant in cases of this nature involving a written contract between two large corporations presumably represented by competent counsel. Such parties should be held to the terms of their written contract whenever it is reasonable to do so, as it is incumbent upon courts to uphold the dignity of a contract whenever possible by preventing parol evidence from being used to negate the terms of written contracts. The First Circuit's words in *Intern. Business Machines v. Catamore Enterprises*, 548 F.2d 1065, 1073 (1st Cir.1976) are particularly apt in this case:

The morass of business dealings between two companies described on this record, their promises oral and written, the disparity of their understandings, the frustration of expectations, the inevitable recriminations and conflicting memories—all this is not unique, new, or infrequently encountered. The law in its effort to facilitate just resolutions of such controversies has, over the centuries, developed certain aids or guides to decision.... The first is the substantive principle that when, in the course of business transactions between people or corporations, free and uncoerced understandings purporting to be comprehensive are solemnized by documents which both parties sign and concede to be their agreement, such documents are not easily bypassed or given restrictive interpretations.

Additionally, as this lawsuit involved a lengthy and complicated fact situation, admitting extrinsic evidence would have increased the possibility of unnecessarily confusing the jury, a possibility section 2–202 is designed to avoid:

But the way [section 2–202] is worded, the trial is certainly not to be a free-wheeling affair in which the parties may introduce before the jury all evidence of terms, including the writing, with the jury then to decide on terms. Rather, it is plain from the rule and from prior history of similar rules that some of the evidence is to be heard initially only by the judge and that he may invoke the rule to keep this evidence from the jury.

WHITE & SUMMERS, *THE LAW UNDER THE UNIFORM COMMERCIAL CODE* 77 (2d ed. 1980). *See also* McCormick, *The Parol Evidence Rule as a Procedural Device for Control of the Jury*, 41 *YALE L.J.* 365 (1932).

In summary, we conclude that the district court’s order barring Presto from introducing extrinsic evidence regarding the intended maximum capacity of the System was not an abuse of discretion as it properly held the parties to the written terms of their contract, accorded with the basic principle of law favoring the dignity of a written contract, and avoided unnecessarily confusing the jury.

Notes and Questions

1. If the parol evidence rule is a substantive rule of contract law, should the Seventh Circuit have treated the question of exclusion *de novo* rather than treated the lower court’s decision with deference?
2. How much does it matter that both parties were commercial entities that were represented by counsel? Should we have our approach to the parol evidence rule depend on the status of the parties? What happened to *contra proferentem*, given that Binks drafted the term sheet? Does it matter that Binks was a smaller company and that the lawsuit was for \$9.5 million?
3. Wasn’t the term sheet a “revised quotation” rather than a completely integrated final agreement? Did Presto have any other arguments it should have tried to get the court to see their parol evidence as “explaining” rather than “contradicting” the revised quotation?

4. Did the court adequately distinguish between the extrinsic evidence that was truly “parol”—the negotiating history—from the “course of performance” evidence? Does § 2-202 justify potentially treating those items of extrinsic evidence differently? The parol evidence was a prior quotation memo submitted by Binks confirming that “4500 pounds of steel work holders will pass through each oven per hour.” The course of performance evidence was that although Binks had recommended that Presto warm the System up and run it up to capacity slowly, Presto had needed to run the System all day right away because Binks’ late delivery had implicated its own ability to meet orders from Sears department store in time for a Christmas rush. The System was operated in this double-loading full-bore way with Binks’ knowledge and without their objection.
5. Notice that the court had to engage in extensive interpretation of the written document before it was able to decide whether to admit the extrinsic evidence. This is not unusual and indeed the two issues—contract interpretation and the parol evidence rule—are often entangled. Speaking of interpretation, the court used two somewhat related canons that we haven’t yet studied. The first, more a generic principle than a rule, is sometimes referred to as *the whole-text canon*, and it, as the name suggests, instructs courts to interpret the contract as a whole. The second, the *rule against surplusage*, suggests that an interpretation which gives an effective meaning to every term of the contract should be preferred. Can you identify where and how the court uses those canons in this case?
6. Didn’t this application of § 2-202 have a Willistonian feel? Does this suggest that Willistonian courts applying a Corbinite statute will use its open-ended provisions to accomplish the objectives it thinks more important than hewing to legislative intent of the UCC drafters? Comments 2 and 3 of 2-202 don’t sound Willistonian, but Willistonian courts may question the bindingness of the official comments and promote their own preferred interpretive regimes on the question of integration and exclusion of evidence.