#47 1/11/74

Memorandum 74-6

Subject: Study 47 - Modification of Written Contracts

BACKGROUND

Civil Code Sections 1697 and 1698 provide:

> 1697. A contract not in writing may be altered in any respect by consent of the parties, in writing, without a new consideration, and is extinguished thereby to the extent of the new alteration.
>
> 1698. A contract in writing may be altered by a contract in writing, or by an executed oral agreement, and not otherwise.

California is one of five states (the others apparently copied our provision) that has a rule comparable to Section 1698.

The Uniform Commercial Code deals with oral modification by providing that a written contract may be modified by an oral agreement unless (1) the modified contract is one required by the statute of frauds to be in writing or (2) the original contract requires that any modification be in writing. The Uniform Code requires that a provision in the original contract requiring that a modification of the original contract can only be made in writing must be separately signed by the parties and the Uniform Code excuses the writing requirement in certain hardship situations. (The text of the Uniform Code provision is quoted on page 1570 of the attached background study.) The Uniform Code provision is based to considerable extent on a similar New York provision that is the result of a series of recommendations by the New York Law Revision Commission.

When California enacted the Uniform Commercial Code, the oral modification provision of the Uniform Code was revised to conform to a considerable extent to Civil Code Section 1698. California is the only state that departs from the official language of this provision of the Uniform Code. The modified version adopted in California was based on the recommendations of

Professors Harold Marsh and William D. Warren, who prepared a background report on the Commercial Code for the Senate Fact Finding Committee on Judiciary.

A background study on this topic, prepared by a part-time, temporary member of the Commission's staff, was published in the Hastings Law Journal in 1972. A copy of the study is attached. We do not attempt to summarize the study here because we believe that it is essential that you read the entire study with some care. Also attached, as Exhibits I and II, are letters concerning this matter from Professor Warren and from Harold Marsh. You should read these letters after you have read the study.

REVISION OF CALIFORNIA COMMERCIAL CODE PROVISION

As noted above, California is the only state that departs from the official language of the Commercial Code provision on modification of contracts. You should note also that both Warren and Marsh consider the only reasonable alternative to the present California Commercial Code provision to be a restoration of the official language of the Uniform Commercial Code in the California Commercial Code. The author of the study, however, recommends a rewriting of the Commercial Code provision.

The staff recommends that the Commission prepare a tentative recommendation to conform the California Commercial Code Section 2209 to the official version of the Uniform Commercial Code. The reasons for this recommendation are well stated in Professor Warren's letter. The California Commercial Code provision is set out on page 1573 of the attached background study; the official version of the Uniform Code is set out on page 1570. The difference between the two versions is in the wording of subdivision (2).

REVISION OF CIVIL CODE SECTION 1698

The more difficult policy decision is what, if anything, should be done with Section 1698. There are a number of alternatives, some of which are listed below.

No Change in Section 1698

The Commission could recommend that no change be made in Section 1698, reporting to the Legislature that the courts have (after many decisions) finally made sense out of the section and that it causes no serious problems as interpreted by the courts. Note, however, the contrast in the analysis of existing law under the section by the author of the background study and by the Warren-Marsh report discussed in the study. In other words, the law is not that clear and understandable.

Repeal Section 1698

The Commission could recommend the repeal of Section 1698 on the ground that the section has generated more litigation than it has avoided and has served as a trap for unwary parties to contracts. Although only a few states (five) have statutory provisions limiting oral modification of a written contract (other than the statute of frauds), the repeal of Section 1698 might create some uncertainty as to what the rule would be in California.

Amend Section 1698 to Adopt Substance of Commercial Code Provision

The Commission could recommend that Section 1698 be amended to adopt the substance of the official text of the Uniform Commercial Code provision. In other words, the section could be revised to adopt the rule that an agreement to modify a written contract need not be in writing unless required by the statute of frauds or by the original contract.

Amend Section 1698 to Conform to the Commercial Code Provision Abolishing the Pre-Existing Duty Rule

Professor Warren suggests that no change be made in Section 1698 except to substitute the Commercial Code provision on consideration (subdivision (1) of Section 2209 as set out on page 1573 of background study). The author of the background study also recommends that this provision of the Commercial Code section be added to Section 1698. The addition of the provision would permit repeal of Section 1697.

Amend Section 1698 to Provide a Clear Statement of the Rule as the Section is Applied by the Courts

The Commission could recommend that Section 1698 be revised to state more accurately the rules developed by the courts in interpreting the section. This would avoid the uncertainty that now exists. Contrast the analysis of the background study with that of the Warren-Marsh study. This is the alternative recommended by the writer of the background study and by the staff.

The writer of the background study sets out his proposed language in amended Section 1698 on page 1584 of the background study. The proposed language, however, does not make any reference to the doctrine of estoppel which is codified in the Commercial Code provision.

The staff recommends that Section 1697 be repealed and that Section 1698 be amended to read:

> 1698. (a) Except as provided in this section, a contract may be altered in any respect by the consent of the parties without new consideration.
>
> (b) An agreement altering any executory portion of a written contract is unenforceable unless the agreement is in writing and signed by the party against whom enforcement is sought.
>
> (c) The requirements of the statute of frauds must be satisfied if the contract as altered is within its provisions.

(d) Although an attempt at alteration does not satisfy the requirements of subdivision (b) or (c), the agreement altering the contract may be enforced to the extent that (1) the party seeking enforcement of the alteration has rendered performance, referable to the agreement, not required by the terms of the written contract or (2) failure to enforce the agreement would be unjust in view of a material change in position in reliance on the agreement.

As an alternative to subdivision (d)--which we believe codifies the holdings of the better reasoned cases under Section 1698--the Commission might wish to use the "waiver" approach of the Commercial Code. See subdivisions (4) and (5) quoted on page 1573. The staff prefers subdivision (d) set out above because it uses the reasoning of the better California cases under Section 1698 but the adoption of the Uniform Commercial Code language would provide uniformity in the "hardship" exception to the nonenforcement rule.

Respectfully submitted,

John H. DeMoully
Executive Secretary

Memorandum 74-6

EXHIBIT I

STANFORD LAW SCHOOL
STANFORD, CALIFORNIA 94305

November 13, 1972

Mr. John H. DeMoully
California Law Revision Commission
Stanford, California 94305

Dear John:

At your request I have read "Modification of Written Contracts in California," 23 Hastings Law Journal 1549-1584 (1972). As I indicated to you, I have no expertise on the subject, and you must read my comments in that light. My conclusion is that I doubt the wisdom of the Commission's undertaking to draft legislation in this field along the lines suggested in the article.

Perhaps I over-simplify the problem of modifications when I say that I see it in terms of three issues: consideration, proof, and relief against hardship. Whether the parties have fully or partially executed or not is relevant to me only when it bears on one of these issues. The emphasis in California on execution seems to put the cart before the horse.

Official Text 2-209 seems an admirable solution of the area and I think the California UCC should be revised to go back to the original version. Certainly subsection (1) resolves the consideration problem correctly in rejecting the old preexisting duty cases. As to the proof problem, my feeling is that so long as the party suing on the modification can prove to the satisfaction of the trier of fact that there was in fact a modification I would as a general principle favor enforcing the modification so long as the Statute of Frauds has been complied with. Thus if the modification is done by a sufficient written memo or if an oral modification satisfies either UCC 2201(3)(a) or (c), the modification should be enforceable to the extent allowed by those provisions, and execution by the parties would be relevant to show compliance with UCC 2201(3)(a) or (c). UCC 2209(4) and (5) seem to give courts the kind of flexibility they need to relieve against hardship that is necessary in this area. Of course, courts will look outside the Code (see UCC 1103) to find other bases for deserved relief when the Code treatment isn't adequate. The only provision of Official Text 2-209 that I'm not entirely pleased with is subsection (2) -- the so-called private Statute of Frauds.

Notwithstanding my reservations about subsection (2), I think California would be wise to restore the wording of Official Text 2-209. We are now the only state not having subsection (2), and the tremendous interstate volume of business in the area of sales transactions calls for a single national rule, particularly on the issue of how forms are written. Whatever the wisdom of California 2209(2), the rest of the nation survives without it, and I am sure that California can do the same. The developing body of case law in other states will be of great assistance to California lawyers in understanding UCC 2209 if our law is made to conform to the Official Text.

The reason California departed from the Official Text originally, as best I can recall, is that Harold and I were presented with a recommendation (which seemed sure to carry) that California reenact section 1698 in place of the Official Text version of 2-209. (This was one of some 1500 recommendations that we were given some six weeks to respond to.) We persuaded the Commission to accept subsection (1) which got rid of the preexisting consideration problem and we got them to accept the rest of 2-209 except for subsection (2). Since section 1698 was sure to be the heart of California 2209, Harold (as best I can recall) believed that the Godbey problem should be clarified. Since there are situations in which unilateral performance of a contract obviously proves nothing about an oral modification, the Commission favored requiring execution on both sides, which after all is probably the literal meaning and legislative intent of section 1698.

If it is desirable to go back to the Official Text version of 2-209, what should be done with section 1698 as to nonsales cases? I would add the substance of subsection (1) of UCC 2209 and leave it as it is. It seems to me that section 1698 as it is currently interpreted is working all right. A large body of case law has been built up around its meaning, and no matter how carefully a restatement of a case law rule is done in a statute it never picks up all the nuances of the case law structure.

My recommendation is vulnerable to the criticism why have two different rules on contract modification in California. My answer to that is that the Legislature when it enacted all the formation of contracts provisions of the UCC decided to have a different law for sales transactions (one uniform throughout the nation) from that prevailing in other contract transactions. The modifications problem should not be treated any differently than are the Statute of Frauds, firm offer, additional terms (Section 2207), etc., issues. The

Legislature has simply decided to have a different law of contract for the sale of goods, and I am not going to challenge their wisdom on that at this late date.

Since the changes in present law that I suggest would involve only a modest change in section 1698 and a change in California 2209 which would entail poaching on the preserve of the California Commission on Uniform State Laws, I doubt that the Law Revision Commission would have great interest in doing what I think should be done. I must admit that the fact the background article cites not one case in California on UCC 2209 in the nearly eight years it has been in force leads me to believe that maybe the problem is not high on a priorities list for law reform. By the way, I am not entirely sure that Mr. Timbie has thought through the relationship between his Godbey restatement and the additional requirement that there be compliance with the Statute of Frauds.

If this letter is of any help to you, I will be as pleased as I am surprised.

Sincerely,

Bill

William D. Warren

WDW:jc

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SCHOOL OF LAW
LOS ANGELES, CALIFORNIA 90024

January 16, 1969

Mr. John H. DeMoully
California Law Revision Commission
School of Law, Stanford University
Stanford, California 94305

Dear John:

In reply to your letter of January 7, 1969 relating to Section 2-209 of the Uniform Commercial Code, my recollection is that the change made in the California statute from the official text was the result of a recommendation made by the State Bar Committee studying the UCC and specifically the subcommittee of that committee which was appointed to review the provisions in Article 2. The comment on this recommendation in our report to the Senate Judiciary Committee was actually prepared by Bill Warren and not by myself, although I concurred in it.

The primary basis for our recommendation as I recall was our belief that requiring the insertion of separate clauses in a contract to be signed separately, as under the New York statute which was essentially copied into the official text of the UCC, is a procedure which has very little to recommend it and merely results in all standard forms incorporating this additional clause. Furthermore, it was our belief that requiring a party to sign or initial a half dozen different printed clauses accomplishes nothing whatever since if he is ready to sign the basic contract he will sign any other number of times that the salesman directs him to. The result is that only where by accident the merchant has failed to get the necessary additional signature does this provision have any meaning, and this does not seem to be a reasonable basis on which to legislate regarding the rights of the parties.

I do not believe that it was any strong feeling about this matter when the code was originally considered, and I would think that there is at least a reasonable chance that no serious opposition would be aroused by a proposal to conform this section into the California code to the official text. However, there is certainly a possibility that the State Bar Committee would again object to the provisions of the official text and also I would imagine a possibility that persons representing retail merchants might finally have become fed up with separate clauses to be signed separately and therefore oppose the change.

My own personal reaction is that the California section is superior but this has to be weighed against the benefits of uniformity, and I would certainly not oppose reverting in this instance to the language of the official text.

Sincerely yours,

Harold

Harold Marsh, Jr.

HM:jr