

Impossibility of Performance Amounting to a Total Failure of Consideration Due to Governmental Action - Montauk Corporation v. Seeds

John D. Alexander Jr.

Follow this and additional works at: <http://digitalcommons.law.umaryland.edu/mlr>



Part of the [Contracts Commons](#)

Recommended Citation

John D. Alexander Jr., *Impossibility of Performance Amounting to a Total Failure of Consideration Due to Governmental Action - Montauk Corporation v. Seeds*, 19 Md. L. Rev. 254 (1959)

Available at: <http://digitalcommons.law.umaryland.edu/mlr/vol19/iss3/9>

This Casenotes and Comments is brought to you for free and open access by the Academic Journals at DigitalCommons@UM Carey Law. It has been accepted for inclusion in Maryland Law Review by an authorized administrator of DigitalCommons@UM Carey Law. For more information, please contact smccarty@law.umaryland.edu.

**Impossibility Of Performance Amounting To A
Total Failure Of Consideration Due To
Governmental Action**

*Montauk Corporation v. Seeds*¹

Defendant Montauk Corporation, a housing developer, constructed a sewage pumping station as a part of its housing project. Defendant accepted plaintiff's offer to service the station upon its completion for a period of five years. Under a local statute, in existence at the time the contract was made, the construction and operation of sewage pumping stations were subject to the supervision and general control of the local Sanitary Commission, the Commission being further empowered to take over such privately owned facilities by purchase or condemnation.² There was no condemnation, but, presumably acting under its statutory power, the Sanitary Commission did decide in this instance to operate the facility itself. The Commission entered into a contract with defendant to operate the station permanently for the same amount of money defendant had promised plaintiff for only five years of service. Plaintiff successfully sued for damages arising from defendant's breach of the executory contract and defendant appealed.³

Defendant-appellant unsuccessfully contended that its breach of contract was the result of governmental action and so was excused by the "frustration" doctrine, *without*

¹ 215 Md. 491, 138 A. 2d 907 (1958).

² MONTGOMERY COUNTY CODE (1955), §74-55.

³ The Sanitary Commission, joined as a third-party defendant, received a jury verdict in its favor. Since no judgment was entered on this verdict, only the relative rights of plaintiff and Montauk Corporation were before the Court on appeal.

regard to the foreseeability of such interference with performance at the time the contract was made.⁴ The Court of Appeals sustained the lower court's instruction, saying:

"The courts have generally held that if the supervening event was reasonably foreseeable the parties may not set up the defense of frustration as an excuse for non-performance. The majority of the courts stress this principle in deciding cases on frustration, and hold that if the parties could have reasonably anticipated the event, they are obliged to make provisions in their contract protecting themselves against it."⁵

The Court's opinion fails to distinguish between impossibility of performance and frustration of purpose. It is submitted that the rules for frustration defenses were applied to a situation where the rules regarding impossibility of performance were appropriate.

In general, a defense of impossibility of performance arises when, though the purpose for which the parties contracted continue unaffected, literal performance becomes impossible. On the other hand frustration of purpose may be a defense where the expected value of performance is destroyed though literal performance remains possible.⁶ While some jurisdictions either fail to make the distinction or deny that it has any operative effect,⁷

⁴ In particular, the appellant objected to the lower court's instruction to the jury:

"... if you find that at the time that the offer of the plaintiff was accepted by the Montauk Corporation that the circumstances were such as to indicate that there was a possibility of interference with the performance by the Commission, and if you further find that the acceptance of the plaintiff's contract by the Montauk Corporation was unconditional, then you are instructed that the risk of such interference is assumed by the Montauk Corporation." *Supra*, n. 1, 499. Though the Court of Appeals was not completely satisfied with the lower Court's instruction, it found no reversible error. *Supra*, n. 1, 500.

⁵ *Supra*, n. 1, 499-500. The Court cited *Contracts — Performance or Breach — Discharge by Impossibility of Performance — Frustration*, 18 *Univ. of Cin. L. Rev.* 535 (1949); *State v. Dashiell*, 195 *Md.* 677, 75 *A. 2d* 348 (1950).

⁶ CORBIN, *CONTRACTS* (1st ed. 1951) §1322; 6 WILLISTON, *CONTRACTS* (Rev. ed. 1938) §1954; 1 RESTATEMENT, *CONTRACTS* (1932) §288; 2 RESTATEMENT, *CONTRACTS* (1932) §§454-469; Smit, *Frustration of Contract: A Comparative Attempt At Consolidation*, 58 *Col. L. Rev.* 287 (1958); Patterson, *Constructive Conditions in Contracts*, 42 *Col. L. Rev.* 903, 943 (1942); *Lloyd v. Murphy*, 25 *Cal. 2d* 48, 153 *P. 2d* 47 (1944); *Raner v. Goldberg*, 244 *N.Y.* 438, 155 *N.E.* 733 (1927).

⁷ *Patch v. Solar Corporation*, 149 *F. 2d* 558, 560 (7th Cir. 1945), cert. den. 326 *U.S.* 741 (1945), where the Court concluded: "Whether you call it impossibility of performance or frustration, the result is the same." This case was one of the few cases cited in the present opinion.

in all cases where there has been some form of interference, courts should distinguish whether literal performance of purpose is interfered with.⁸

Both the frustration of purpose and the impossibility of performance defenses, being based ultimately upon equitable considerations, conflict with the certainty of contract which the law aspires to.⁹ Ordinarily unqualified promises result in absolute liability. Confronted with the conflict between the equities of a hardship case and the general aims of contract law, the Courts display an understandable lack of uniformity in their decisions.¹⁰ Furthermore, the formulation of rules of general application for impossibility and frustration defenses is complicated by the fact that these defenses extend *in theory* to all the various areas of contract law while *in practice* various areas of commercial law are treated as distinct through usage, case law or statute.¹¹ Nevertheless, in situations where governmental interference is present, most courts require that a frustration defense be premised upon a show-

⁸ 1 RESTATEMENT, CONTRACTS (1932) §288:

"Where the assumed possibility of a desired object or effect to be attained by either party to a contract forms the basis on which both parties enter into it, and this object or effect is or surely will be frustrated, a promisor who is without fault in causing the frustration, and who is harmed thereby, is discharged from the duty of performing his promise unless a contrary intention appears."

Admittedly this section is at best a vague and uncertain guide as to when the rules of frustration should be applied. Under the facts of the Coronation Cases, *Krell v. Henry*, [1903] 2 K.B. 740, set out by the Reporter as Illustration 1, this section assumes a clarity which vanishes upon an attempt to apply this abstract of the law to other particular instances. 6 CORBIN, CONTRACTS (1st ed. 1951), §1322, especially note 19, and Smit, *Frustration of Contract: A Comparative Attempt at Consolidation*, 58 Col. L. Rev. 287, 309 (1958) are critical of this section. Nevertheless, these rules should only apply in cases where literal performance remains possible on both sides.

⁹ Gow, *Some Observations on Frustration*, 3 Int. & Comp. L.Q. 291 (1954); *British Movietonews Ltd. v. London and District Cinemas Ltd.*, [1951] 1 K.B. 190. On appeal, [1952] A.C. 166, the House of Lords was sharply critical of the King's Bench's frank admission that the Courts in fact do remake contracts. 6 CORBIN, CONTRACTS (1st ed. 1951) §1331; 6 WILLISTON, CONTRACTS (Rev. ed. 1938) §1937.

¹⁰ See Note, *The Fetish of Impossibility In the Law of Contracts*, 53 Col. L. Rev. 94 (1953) which convincingly maintains that the technical rules of impossibility are not followed by the Courts and that underlying factors of social justice and public policy control the decisions. For example, the result in the subject case, taking a broad equitable view, can be justified on the grounds that defendant benefited from the contract it entered into with the Sanitary Commission and that perhaps its conduct was voluntary. Notice also that plaintiff was completely without fault.

¹¹ For example sales of goods and employment contracts under the same operative facts may be treated differently than construction contracts. Bankruptcy, by far the most important impossibility defense known to the law, is exclusively a matter of statute.

ing of severe hardship.¹² Furthermore the frustration cases generally hold that frustration caused by reasonably foreseeable supervening events is no defense.¹³ On the other hand most courts do not require these elements in impossibility cases and those that do are much less strict.¹⁴

If such a distinction is to be made between the two defenses and their consequences, classification becomes important in a case such as the present where the party asserting the defense relies on the fact that the other party's performance has become impossible. Defendant housing developer's own promise to pay money has not become impossible of performance. However, the impossibility of plaintiff's performance (to service the facilities) has resulted in a total failure of the consideration moving to defendant. Defendant should be excused from the performance of his counter promise.

Frustration cases are properly strict for the following reasons: (1) since literal performance remains possible on both sides, the party seeking to be excused has received, or if not excused, will receive literally what he bargained for, and since most contracts contain the possibility of loss as well as benefits, it is not clear why a contracting party should be allowed to avoid the losses, yet reap the benefits; (2) it is difficult to determine what degree of frustration the law should recognize and once a test be established, difficult to apply the test to any given set of facts.

Applying this rationale to a case such as the present, where impossibility has resulted in a total failure of consideration to the party seeking to be excused, it appears that the less rigorous requirements of the law of impossibility are more appropriate since: (1) the party seeking to be excused will not receive the performance he contracted for; (2) the loss is total and easy to determine, since it amounts to failure of the performance promised to the party who seeks the excuse; (3) the party who asserts the defense can fairly be excused since the opposite party cannot, and need not perform, and no benefit can accrue to the party asserting the defense. On the facts

¹² Compare the frustration cases of *Lloyd v. Murphy*, 25 Cal. 2d 48, 153 P. 2d 47 (1944) and *Standard Brewing Co. v. Well*, 129 Md. 487, 99 A. 661 (1916) with *Baltimore Luggage Co. v. Ligon*, 208 Md. 406, 417-418, 118 A. 2d 665 (1955) an impossibility case adopting 2 RESTATEMENT, CONTRACTS (1932) §454, where "impossibility" is defined as including ". . . not only strict impossibility but impracticability because of extreme and unreasonable difficulty, expense, injury or loss involved."

¹³ For an excellent discussion see *Lloyd v. Murphy*, *ibid.*, and cases cited.

¹⁴ See *Lloyd v. Murphy*, *supra*, n. 12, and the Maryland cases of *Wischusen v. Spirits Co.*, 163 Md. 565, 163 A. 685 (1933) and *State v. Dashiell*, 195 Md. 677, 75 A. 2d 348 (1950), hereinafter discussed, *infra*, *circa* n. 16.

of the present case, it seems clear that Montauk could not recover damages from Seeds for Seeds' failure to service the facilities, and it is difficult to see why one party to a contract may be allowed an impossibility defense based upon the impossibility of his own literal performance and yet the other party to the contract is still held.¹⁵

The Maryland case of *Wischhusen v. Spirits Co.*,¹⁶ like the present case, involved a situation where the party charged defended on the ground of total failure of consideration. At the time defendant distillery hired the plaintiff to manage certain of its operations, a government permit, dependent in part upon the skill and character of distillery employees, was required. The government refused the permit because the plaintiff was not trustworthy or competent. The Court excused the defendant from its promise to pay wages, saying:

"[A] sufficient defense to the plaintiff's demand is that no person shall call upon another to perform his part of the contract until he himself has performed . . . all that he has stipulated to do as the consideration of the other's promise."¹⁷

In both the *Montauk* and *Wischhusen* cases, the breach was of an executory contract; neither party had substantially changed its position, and there was a total failure of consideration moving to the charged party. In the *Wischhusen* case, the acts of the plaintiff caused the failure of performance. If the failure has been caused by a third person or other forces not within the control of either party, there is no reason why the charged party should not likewise be excused.¹⁸ In the *Montauk* case for example, while the plaintiff lost the value of his bargain through no fault of his own, the defendant never received any benefit moving from the plaintiff. Of course, if defendant in any way contributed to or brought about the interference, it

¹⁵ 6 CORBIN, CONTRACTS (1st ed. 1951) §261, criticizes the failure of the Restatement to similarly distinguish, saying:

"Although it is perfectly clear that failure of the consideration . . . is a 'frustration' of the purpose or object for which he entered into the contract, *whether it is due to a wrongful breach or to an excusing impossibility*, the Institute says nothing about 'frustration' either in the sections dealing with Impossibility or in those dealing with Failure of Consideration." [Emphasis added].

See also the text that follows and especially n. 19 to §1322. The present writer suggests that though the term frustration accurately describes the situation of the charged party, to avoid ringing in the strict rules of frustration the term impossibility of counter-performance would be more appropriate.

¹⁶ 163 Md. 565, 163 A. 685 (1933).

¹⁷ *Ibid.*, 571.

¹⁸ See the quotation from Corbin, *supra*, n. 15.

should not be excused. Thus, the sole issue in the present case should have been whether the defendant, by entering into the contract with the Commission, *voluntarily* caused plaintiff's performance to become impossible.¹⁹

The remainder of this casenote discusses to what extent lack of reasonable foreseeability of interference should be a prerequisite to excuse in cases where the impossibility of performance causes a total failure of consideration to the party charged. The two Maryland decisions cited in the present opinion modify the requirement of foreseeability. In *Wischhusen v. Spirits Co.*,²⁰ after excusing the defendant because of total failure of consideration, the Court stated as an alternative ground for its decision, the modern rules of impossibility of performance and adopted the view of the RESTATEMENT.²¹ At the time the contract

¹⁹ Patterson, *Constructive Conditions In Contracts*, 42 Col. L. Rev. 903, 943 (1942). Some Courts, influenced by policy considerations, do not require that a charged party strenuously resist governmental interference. *Baily v. De Crespigny*, [1869] 4 Q.B. 180; *Mawhinney v. Millbrook Woolen Mills*, 234 N.Y. 244, 137 N.E. 318 (1922); *cf. Wilson & Co. v. Curlett*, 140 Md. 147, 117 A. 6 (1922); *Autry v. Republic Productions*, 30 Cal. 2d 144, 180 P. 2d 888 (1947). The Court in the present case did not allow Montauk to introduce evidence that the Sanitary Commission's offer to negotiate was, in view of its power of condemnation and the facts of the case, a coercion which absolved defendant of any voluntary contribution to the impossibility. In *Dorsey v. Oregon Motor Stages*, 183 Ore. 494, 194 P. 2d 967, 983 (1948), a case whose operative facts are similar to the Montauk case, evidence of coercion and duress was allowed. Both the majority and dissent [dis. op. 984] in the Dorsey case adopted the reasoning of *Wischhusen v. Spirits Co.*, *infra*, n. 20. The dissent, distinguishing, the *Wischhusen* case on its facts, said, ". . . [I] think duress, coercion and governmental authority in that case was doubly distilled" [985].

²⁰ 163 Md. 565, 163 A. 685 (1933).

²¹ *Ibid.*, 572-573.

"The general rule with respect to contracts is generally stated to be that, when the impossibility of performance arises after the formation of the contract, the failure of the promisor to perform is not excused, whether such impossibility was absolute or relative, or whether owing to the fault of the promisor or not, upon the theory that, if the promisor makes his promise unconditionally, he takes the risk of being held liable even though performance should become impossible by circumstances beyond his control. * * * The unfair consequences of this rule resulted in exceptions when the impossibility arises (1) either from a change in domestic law or by an executive or administrative order; (2) or when the thing, whose continued existence is essential to the performance of the contract, is destroyed without fault of either party to the contract; . . ."

The Court then quoted 2 RESTATEMENT, CONTRACTS (1932) §458:

"Supervening Prohibition or Prevention by Law: A contractual duty or a duty to make compensation is discharged in the absence of circumstances showing either a contrary intention or contributing fault on the part of the person subject to the duty, where performance is subsequently prevented or prohibited . . . (b) by a judicial, executive or administrative order made with due authority by a judge or other officer of the United States, or of any one of the United States."

This case and the Restatement were cited with approval in *Fast Bear. Co. v. Precision Dev. Co.*, 185 Md. 288, *circa* 307, 44 A. 2d 735 (1945). See also 6 WILLISTON, CONTRACTS (Rev. ed. 1938) §1939.

was entered into, both parties knew that a governmental authority had the power to interfere with the contract. The Court took the position that the charged party should be bound to his unqualified promise only if it was reasonably foreseeable that this existing power would be exercised.²² The other Maryland case cited is *State v. Dashiell*,²³ where plaintiff-owner, who had brought suit for a declaratory decree establishing an impossibility defense, was not excused from paying damages sustained by the building contractor when construction was delayed by failure to obtain clearance from the appropriate federal authority. The Court said:

“Thus, in those cases where a regulation of an administrative agency is already in force at the time of the formation of the contract, the decisive question is whether or not the promisor assumed the risk of interference by the regulation.”²⁴

The Court held that by *the express terms of its contract*, plaintiff recognized and assumed the risk of getting the permit. If, when the contract is made, there exists a governmental authority having the power to interfere with the contract's performance, these cases require an affirmative showing of assumption of risk before a party will be bound to his unqualified promise.²⁵ It should be noted that both these cases present a stronger basis for an assumption of risk through silence than is present in *Montauk*. Both cases involved situations where governmental action, the issuance of permits or licenses, was a known prerequisite

²² *Ibid.*, 570: “The stipulations of the contract must therefore be construed to have implicit reference to a continuing lawful manufacture. . . . The refusal of the necessary permit was therefore a subsequent, unanticipated, circumstance, in connection with which the contract must be construed. . . .”

²³ 195 Md. 677, 75 A. 2d 348 (1950).

²⁴ *Ibid.*, 689.

²⁵ Both the *Wischhusen* and *Dashiell* cases cited *Anglo-Russian Merchant Traders v. Batt & Co.*, [1917] 2 K.B. 679, 686 where at the date of the contract for sale and shipment of goods both parties knew that a government license would be necessary to enable the defendant-shipper to perform. The contract was silent as to assumption of risk. The Court excused the shipper saying: “I cannot agree that, in order to give to the contract its business efficacy, it is a necessary implication that the sellers undertook an absolute obligation to ship whether a licence was or was not obtained.” *Accord*: *P. Dougherty Co. v. 2471 Tons of Coal Ex Barge Annapolis*, 278 F. 799 (D.C. Mass. 1922), where the Court decided that the fact that both parties knew at the time of the contract that the subject matter of the contract was under government control did not bar an impossibility defense. But compare *Inter-Coast S. S. Co. v. Seaboard Transp. Co.*, 291 F. 13 (1st Cir. 1923), also cited in the *Dashiell* case, where on essentially the same operative facts as in *Anglo-Russian* the shipper was not excused.

to any performance on the contract. Usually in such situations, one party has expressly or by clear implication assumed the affirmative duty to obtain the prerequisite clearance. Such a duty does not exist in a *Montauk* situation where there was no prerequisite governmental action, the government having instead a general power to intervene by purchase or condemnation.

The view of the *Wischhusen* and *Dashiell* cases is expanded and applied in *L. N. Jackson & Co. v. Royal Norwegian Government*,²⁶ where the District Court refused to excuse the promisor-shipper because the supervening impossibility, a government war-time order, had been foreseeable at the time the contract was made. The Circuit Court, in reversing the lower Court, said:

“This approach practically puts the burden upon the promisor to show non-foreseeability. Carried to its logical limits such a view would practically destroy the doctrine of supervening impossibility, notwithstanding its present wide and apparently growing popularity. * * * In fact, the more common expression of the rule appears to be in terms which tend to state the burden the other way, e.g., that ‘the duty of the promisor is discharged, unless a contrary intention has been manifested’ or ‘in the absence of circumstances showing either a contrary intention or contributing fault on the part of the person subject to the duty.’ * * *

“Whether or not these authorities go so far as to state a definitive rule of preferred interpretation, they do certainly suggest that, where the external circumstances present a case for the fair operation of a rule excusing performance, that shall not be denied unless the fault in not providing against it seems clear and unilateral.”²⁷

²⁶ 177 F. 2d 694 (2nd Cir. 1949), cert. den. 339 U.S. 914 (1950).

²⁷ *Ibid.*, 699. The lower court opinion, *L. N. Jackson Co., v. Lorentzen*, 83 F. Supp. 486 (S.D.N.Y. 1949), applying the foreseeability rule, was commented upon favorably in a Note, *Contracts—Performance or Breach—Discharge by Impossibility of Performance—Frustration*, 18 Univ. of Cin. L. Rev. 535 (1949). This note was one of the few authorities cited by the Court in the *Montauk* case, *supra*, n. 1, 500. In rejecting the strict foreseeability rule, the Circuit Court opinion is in agreement with *L. N. Jackson & Co. v. Seas Shipping Co.*, 185 Misc. 94, 56 N.Y.S. 2d 501 (1945), *aff'd.* without opinion 270 App. Div. 830, 61 N.Y.S. 2d 371 (1946), and by the Court of Appeals, 296 N.Y. 529, 68 N.E. 2d 605 (1946), motion for reargument den. 69 N.E. 2d 565 (1946), a case arising out of the same facts. *Accord:* *Badhwar v. Colorado Fuel and Iron Corporation*, 138 F. Supp. 595, 607 (S.D. N.Y. 1955) *aff'd.* on other grounds 245 F. 2d 903 (2nd Cir. 1957); *Johnson v. Atkins*, 53 Cal. App. 2d 430, 127 P. 2d 1027 (1942). See also cases cited *supra*, n. 25. This rule should apply both to impossibility of performance and total failure of consideration cases.

The "reasonably foreseeable" rule is a fiction of law. Under this rule, a promisor is bound if it was reasonably foreseeable that governmental action would interfere with the performance of the counter promise. If his promise is unqualified, the law considers that the promisor has in fact considered the possible contingencies as a reasonably farsighted individual and that consequently his silence constitutes an assumption of risk.²⁸ By creating what are in effect presumptions, fictions such as this serve the useful function of establishing norms by which the community can conduct its affairs. Especially in contract law, it is necessary that the effect of promises be predictable. If, however, the fiction chosen by the law significantly differs from the understanding of the majority of contracting parties (usually the fictions of law, for better or worse, linger behind) confusion and injustice result.²⁹

A "reasonable" businessman of today, who, at the time of contracting, knows there exists a governmental agency with the power to *interfere* with the performance of the contract, would, if confronted, in some words or other give effect to the rule of dependency of promises, e.g., "If you can't do the job because of the government, I won't have to pay, etc." Though admittedly as much a fiction as the older view, the rule in Maryland today should be that in the absence of accompanying facts, usages, or express terms showing an intention to assume the risk of non-performance, impossibility of performance due to governmental action excuses not only those performances literally interfered with but also all cross promises.

JOHN D. ALEXANDER, JR.

²⁸ Gow, *Some Observations on Frustration*, 3 Int. & Comp. L.Q. 291 (1954); Smit, *Frustration of Contract: A Comparative Attempt at Consolidation*, 58 Col. L. Rev. 287 (1958).

²⁹ The rule of absolute liability for unqualified contractual undertakings is a corollary to the principle of freedom of contract. In *Taylor v. Turley*, 33 Md. 500, 505 (1871) it was said: "It is not the province of the Courts to interfere with the natural rights of parties to contract. . . ." The Court concluded: ". . . folly, weakness, or want of judgment, will not necessarily defeat a contract." Today, however, the ability to contract is more dependent than ever on forces external to the parties. The development of the interest of the state in contracts and their subject matter, as evidenced by the proliferation of regulatory agencies and the increased exercise of the power of eminent domain, compels today's businessman to employ extraordinary caution in contracting. Should the Courts hold him and his counsel to the same kind of foresight possible in the time of laissez-faire economy? In the *Kronprinzessin Cecille*, 244 U.S. 12, 24 (1917), Holmes, J. said:

"Business contracts must be construed with business sense, as they naturally would be understood by intelligent men of affairs."