



When is there an agreement to build: The principles involved during contract formation

November 19, 2007 - Spotlights

In an action arising out of the construction of a hangar for Jet Blue at Kennedy Airport, a divided New York intermediate appellate court found no agreement to build had ever existed when it granted the general contractor's motion to dismiss a subcontractor's complaint for breach of contract. The key to the decision was the "inception clause" in the proposed contract documents. The agreement was never signed by the general contractor.

The "inception clause" provided that the contract would not be binding on the general contractor "unless and until" the general contractor executed the document. The subcontractor "was not obligated to perform work until "the general contractor" executed the subcontract. The inception clause further provided that if the general contractor failed to return the fully executed contract by a certain date, the subcontractor could walk away from the obligation.

The clause added, "In such event neither [the general contractor] nor the subcontractor shall have any liability to the other and [the general contractor] shall have no liability to make payment for work performed by subcontractor, if any, or for anticipated profits." Finally, the clause provided, "subcontractor shall not be obligated to perform work until [general contractor] executes the subcontract."

Notwithstanding its clear knowledge of the terms of the inception clause, the subcontractor began work on the subcontract. After receiving the general contractor's oral advice that it had been awarded the contract, both the subcontractor and general contractor traveled to Texas for a "kickoff meeting" at which "a substantial amount of design development and coordination was accomplished."

On a motion to dismiss, the court is required to treat plaintiff's pleaded allegations as true before deciding whether, as a matter of law, the complaint fails to state a legally recognizable cause of action. Here, plaintiff alleged that even while the general contractor had been meeting with the subcontractor, it was sharing the subcontractor's work product with another subcontractor in an effort to induce it to take over that subcontractor's work. Despite this allegation, the appellate court ruled that the courts of New York "will give effect to a party's clearly stated intention not to be contractually bound until it has executed a formal written agreement." The court stated, "when a party gives forthright, reasonable signals that it means to be bound only by a written agreement, courts should not frustrate that intent."

The subcontractor argued that the general contractor's actions and oral statements clearly showed that the general contractor had waived the plain language of the "inception clause" and, therefore, that an agreement had been formed. The majority disagreed. It stated that the "inception clause" was the general contractor's "pre-contractual notice to [the subcontractor] of what would constitute the [general contractor's] 'manifestation of assent' to a binding agreement between the parties." The

court found no waiver had occurred.

Finally, the court dismissed that portion of the subcontractor's complaint that sought compensation for the fair and reasonable value of the subcontractor's work. Given the clear language of the inception clause, the subcontractor could not have reasonably relied on the general's oral advice that it had been awarded the subcontract, should not have traveled to Texas for the kick-off meeting or performed any design work. Because of the clear language of the "inception clause" it was not entitled to any payment for the work it had performed.

The lengthy, vigorous dissent found that the contradictory signals given by the general contractor negated the "extravagant sweep of the majority's reading of the 'inception clause.'" The dissent argued that the general contractor's statements and actions despite its knowledge of the terms of the "inception clause," which it drafted, should have been sufficient to enable the complaint to withstand a motion to dismiss.

Analysis. The majority's stated goal in reaching its decision was to preserve New York's strong public policy in favor of "freedom of contract." This freedom includes the parties' freedom "to avoid oral agreements." The majority's reluctance to make a contract "by judicial fiat" where one was not intended continues a long-established judicial reluctance to interfere with contract formation where both parties, for whatever the motivation and despite their actions, do not want the contract to come into existence.

To its credit, the majority acknowledged that the general contractor's actions, "if the allegations of the complaint are true, leave much to be desired." It noted that had the complaint been based on different equitable theories, it would "likely reach a considerably different result." The majority subordinated its acknowledgment of the reality of the parties' actions to its view that the strong policy of freedom of contract compelled it to follow the "rules of engagement" created by the "inception clause."

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