

The Perils of the Statute of Frauds

“But we shook on the deal,” Paul Plumber explained to his lawyer. “There were at least five witnesses. After we agreed on the terms of the transaction, Bob Smith, CEO of Owner X, shook my hand, and then the two of us went out for drinks with our people to celebrate.”

“Did both of you sign any form of agreement?” asked the lawyer.

“No,” replied Paul. “What were we supposed to do? Scribble it out on the back of a cocktail napkin?”

Perhaps that might have helped. This fictitious exchange took place after Mr. Smith denied ever entering into a contract with Paul. Mr. Smith claimed that he was just negotiating with Paul; if they had a deal, they would have signed a contract. A few days after the parties’ meeting, Mr. Smith did in fact sign an agreement—with Carl Competitor for the same scope of work that Paul had offered, but at a lower price.

After learning that Owner X entered into an agreement with Carl Competitor, Paul went to his attorney to inquire about filing a lawsuit for breach of contract. The lawyer had to determine whether the parties had a contract, and if so, could Paul enforce it? The answer, like most things in the law, depends primarily on the facts. It also depends on the application of the facts to a long-time statutory defense to contract enforcement, the Statute of Frauds.

For purposes of this discussion, let’s assume that the parties *did* have a contract. They had the requisite offer, acceptance, consideration, and meeting of the minds on all essential terms. The only thing they did not have was a written document memorializing their deal. Could Paul enforce their oral agreement? Again, the answer depends squarely on the application of the Statute of Frauds.

WHAT IS THE STATUTE OF FRAUDS?

The Statute of Frauds originally was passed by the English Parliament in 1677, and it forms the basis of most modern laws requiring that certain agreements be in writing to be enforceable. As the late contracts scholar Professor Samuel Williston explained, “The Statute of Frauds was designed to prevent the enforcement of unfounded fraudulent claims by requiring written evidence.”

The Statute of Frauds was re-enacted on a state level throughout the United States; however, its precise contours vary from state to state. For this reason, it is critical that you understand the specific requirements of the Statute of Frauds that governs your business agreements. While I am loathe to make any generalizations about the Statute of Frauds, it is fair to say that most jurisdictions require four types of agreements to be in writing: contracts to assume the obligation of another, contracts that cannot be performed within one year, contracts for the sale of land, and contracts for the sale of goods. The Statute of Frauds is satisfied by

the existence of a written memorandum signed by the party (or parties) to be charged and sufficiently indicating the terms of the parties’ oral agreement.

Assuming that the applicable law in Paul’s jurisdiction requires only a writing for the above-mentioned four types of agreements, one must analyze the facts surrounding Paul’s agreement with Mr. Smith. If the parties’ agreement does not require the assumption of another’s obligation, is capable (by its terms) of being performed within one year, does not involve the sale of land, and does not involve the sale of goods (assuming it was for performance services only), then the Statute of Frauds is not a defense to the enforcement of the agreement. In other words, under these facts Paul Plumber and Owner X have an enforceable, oral agreement (without the need for a written memorandum).

Of course, this conclusion does not make Paul’s lawsuit against Owner X any easier. He still bears the burden of proving the agreement in court. While he has at least five witnesses, who knows what they will remember and testify to under oath?

GET IT IN WRITING

The moral of the story here is to consult with your attorney and have your business agreements reduced to an appropriate writing signed by the parties’ principals or authorized representatives. This eliminates the possibility of one party raising the Statute of Frauds as a defense to the enforcement of the agreement. It also eliminates the possibility of having to rely on witnesses to prove the existence of the agreement.

FOR EXAMPLE

In *J&J Plumbing & Heating, LLC v. Tate*, the plaintiff plumbing contractor learned the hard way about the ramifications of the Statute of Frauds. J&J filed a breach of contract action against former employees of the company based on an alleged 2003 oral agreement to purchase “the entire business of Plaintiff to include all of the inventory, equipment, and accounts receivable.” The complaint alleged that the agreement required the defendants to pay Wiegman (one of J&J’s principals) \$60,000 at the rate of \$300 per week and to pay Wiegman’s truck payment until the loan on the truck was paid off. The defendants would become responsible to pay the trade credit owed by J&J in the approximate amount of \$50,000. Defendants also would be responsible for keeping current all of the bills in the normal course of business, including federal, state, local, and employee withholding taxes.

After the defendants failed to pay the trade credit, business taxes, employee withholding taxes, and truck loan payments, the plaintiffs sued them for breach of contract. Based on the defendants’

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failure to make these payments, as well as their alleged failure to pay outstanding federal tax and trade credit liabilities, the plaintiffs sought almost \$400,000 in damages.

The defendants moved for summary disposition of the complaint, arguing that the parties' agreement was within Michigan's Statute of Frauds (and was required to be in writing) because it was not capable of being performed within one year.

A SAMPLE STATUTE OF FRAUDS

Michigan's Statute of Frauds (M.C.L. §566.132)—a good representative sample Statute of Frauds—provides, in pertinent part:

1. In the following cases an agreement, contract, or promise is void unless that agreement, contract, or promise, or a note or memorandum of the agreement, contract, or promise is in writing and signed with an authorized signature by the party to be charged with the agreement, contract, or promise:
 - a. An agreement that, by its terms, is not to be performed within one year from the making of the agreement
 - b. A special promise to answer for the debt, default, or misdoings of another person
 - c. An agreement, promise, or undertaking made upon consideration of marriage, except mutual promises to marry
 - d. A special promise made by a personal representative to answer damages out of his or her own estate
 - e. An agreement, promise, or contract to pay a commission for or upon the sale of an interest in real estate
 - f. An assignment of things in action, whether intended as a transfer for sale, for security, or otherwise
 - g. An agreement, promise, contract, or warranty of cure relating to medical care or treatment. This subdivision does not affect the right to sue for malpractice or negligence.

BACK TO THE EXAMPLE...

Here, the Michigan Court of Appeals agreed with the defendants and affirmed the dismissal of the lawsuit under M.C.L. 566.132(1)(a). As the court explained: "The alleged oral contract required that defendants pay \$60,000 in \$300 weekly installments. Therefore, by its terms, it comes within the statute of frauds." The court rejected the plaintiff's argument that it was technically possible for the agreement to be performed within one year (if, for example, the plaintiff prepaid the \$60,000). "It is not enough that one can imagine some turn of events whereby the contract could be fulfilled within one year. Rather, the terms of the contract must show that it is capable of being performed within one year. By its terms, the parties' alleged agreement was to be performed over 200 weeks' time, or nearly four years, and there was nothing in the terms [of the agreement] to indicate that it could be performed within one year (e.g., pay \$60,000 in two years or less or pay \$60,000 in two years or on demand)."

The *J&J Plumbing* case illustrates the result that could visit a party who ignores the Statute of Frauds and does business solely with handshakes and verbal agreements. Such a party conducts business at their peril. While the example of Paul Plumber indicates that it certainly is possible to conduct business this way, the example of *J&J Plumbing* demonstrates the harsh ramifications that may result. **PSD**

RECOMMENDED READING

9 Samuel Williston & Richard A. Lord, *A Treatise on the Law of Contracts* § 21:1 (4th ed. 1999).

J&J Plumbing & Heating, LLC v. Tate, Nos. 277824, 279838, 2008 WL 4891807 (Mich. Ct. App. Nov. 13, 2008).



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