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Right of Contribution By One Jointly Settling Defendant Against Another

This week we take a double dip into cases from the Court of Appeals of Indiana. The first case for our provides an interesting scenario and delves into interesting issues of contract formation along with providing a useful, albeit moot (in the classical sense, i.e., "[o]pen to argument; debatable"). The second case we will discuss in a subsequent post we look at for the limited issue of when a trial court may be reversed on appeal for denying a motion to amend a complaint.

Our first case of the day is *New v. T3 Investments Corp*. We need not delve too deeply into the facts of the case. In short, a bank made a loan to a company that was secured by real property and personal guaranties of several companies and persons. The company defaulted on the loan and the bank sought to foreclose on the property. The guarantors entered into a settlement agreement with the bank and the property was sold. After the sale, there was still an $865k deficiency. One of the guarantors, T3, paid the entire deficiency then brought suit against the other guarantors for contribution, seeking to recover a pro rata share from each. The guarantors tried to avoid paying their due by invoking a provision in the settlement agreement with the bank. It stated:

> 10. **Mutual Release**. With the sole exception of the rights granted to the Bank under this Agreement, which shall survive unless Payment is made as set forth herein, the Bank, Hillcrest, and the Guarantors, for

> themselves, their predecessors, successors, parent companies, affiliates, partners, members, heirs, representatives, assigns and all other persons or entities, do hereby fully, unconditionally and irrevocably waive as against, and release, one another, and all of their officers, directors, stockholders, partners, members, parents, affiliates, employees, agents, representatives, attorneys, predecessors, successors and assigns, of and from any and all actions, causes of action, claims, demands, damages (including without limitation compensatory or punitive damages) defenses, counterclaims, setoffs of any kind, costs, penalties, attorneys fees or expenses, whether known or unknown, whether contingent or liquidated, whether in contract, tort, statute or under any other legal theory, arising out of or related to, the Loan and in connection with any act or omission by any party, and including without limitation, the claims and counterclaims which are the subject of the Foreclosure Lawsuit and the Guarantor Lawsuit.

Based upon the release language, the remaining guarantors argued that they were not liable to T3 for contribution because "each party agreed to waive and release any and all claims . . . against one another and that such mutual promises constitute sufficient consideration." Read in isolation and in its most literal sense, the language would appear to support the remaining guarantors. The trial court and the court of appeals disagreed. The trial court granted summary judgment to T3 and the remaining guarantors appealed.

On appeal, the court delved into a fairly intricate analysis of contract formation. I will note that a few weeks ago, I disagreed with a dissent from Judge Brown. But, as I constantly remind, we have particularly skilled judges in Indiana and Judge Brown is no exception. She is the author of this week's case and provides a truly remarkable analysis of contract formation. Although the question is one of contract formation–requiring the existence of an offer, the acceptance of that offer, and consideration (the magical legal requirement that turns a promise from a gratuitous promise to one that is enforceable)–the court did not need to delve into every aspect of formation, only consideration was at issue.

The remaining guarantors, citing cases in support, argued "that a promise for a promise constitutes consideration," and "'mutual release within a settlement agreement is sufficient consideration <u>in and of itself</u> to render'" such release enforceable as a matter of law." T3, to the contrary, argued "that the only consideration contemplated by the parties under the Settlement Agreement concerned the Bank receiving a payment of approximately $2.2 million in exchange for it dismissing the Guarantor and the Foreclosure lawsuits." In resolving the issue, the court recognized:

> Contracts are formed when parties exchange an offer and acceptance. "The basic requirements are offer, acceptance, consideration, and 'a meeting of the minds of the contracting parties.'" "To constitute consideration, there must be a benefit accruing to the promisor or a detriment to the promisee." "A benefit is a legal right given to the promisor to which the promisor would not otherwise be entitled." "A detriment on the other hand is a legal right the promisee has forborne." "The doing of an act by one at the request of another which may be a detrimental inconvenience, however slight, to the party doing it or may be a benefit, however slight, to the party at whose request it is performed, is legal consideration for a promise by such requesting party." "In the end, consideration—no matter what its form—consists of a bargained-for exchange."

Using this standard, the court looked to the settlement agreement and noted right up front that the "guarantors negotiated from the same position" in the settlement. Specifically, "the Settlement Agreement throughout refers to the Guarantors as one entity." Looking at the agreement in this light, it was clear that there was no bargained for exchange, necessary for consideration, between the guarantors themselves; "[t]he bargained-for exchange concerned the Loan . . . and the two lawsuits the Bank had filed, and the parties made an agreement as to how to resolve those specific issues." It is a conclusion that is remarkable in its simplicity.

Now we turn to the second part of our discussion: the voluntary payment doctrine. This is not the first time we've discussed the voluntary payment doctrine, and as our frequent readers may remember, I am the author of a comprehensive journal article on the subject: *Practitioner's Guide to the Voluntary Payment Doctrine*. Before examining the scenario put forward here, I will note that there are two doctrines of law, both defenses to otherwise just claims, which I abhor as perversions of justice. The first is the voluntary payment doctrine; the other is the puffery defense, which, of course, we've discussed, and is well discussed in an appropriately titled article: *Legal Tolerance Towards the Business Lie and the Puffery Defense: The Questionable Assumptions of Contract Law*.

In footnote 2, the court delved very briefly into the doctrine. The language is purely obiter dictum as the court found the argument untimely, since it was first made in a motion to reconsider. Nevertheless, and despite very little analysis, the court's almost intuitive conclusion is correct and, therefore, merits a little discussion. Here is footnote 2 in its entirety (minus the citations):

> The Appellants also argue that T3's claim is barred by the voluntary

> payment doctrine. However, that argument was not raised until they filed their motion to reconsider. The trial court was free to disregard this issue, which was not properly preserved for appeal. Further, as noted above T3 paid the deficiency pursuant to an order of garnishment contained in the Deficiency Order. The Indiana Supreme Court has stated that the voluntary payment rule
>
> > is that money voluntarily paid in the face of a recognized uncertainty as to the existence or extent of the payor's obligation to the recipient may not be recovered, on the ground of 'mistake,' merely because the payment is subsequently revealed to have exceeded the true amount of the underlying obligation.
>
> We cannot say that the voluntary payment doctrine applies under these circumstances.

That standard stems from the 2004 Indiana Supreme Court case *Time Warner Entertainment Co., L.P. v. Whiteman*. The standard utilized in *Whiteman* is quite different from the traditional enunciation of the voluntary payment doctrine–that money cannot be reclaimed where it has been paid with full knowledge of the facts though the recipient was not legally entitled to payment. Under this traditional approach, the doctrine would prohibit a subsequent action for contribution, depending on whether the defendants liability to the plaintiff was joint or by apportionment. A good example is an early twentieth century case from the Supreme Court of Virginia: *Briggs v. Barnett*. There, the court recognized that if the parties are jointly liable, then the payment of the full amount by one party does not prevent a claim for contribution against the other. But, if the parties were separately liable for a portion, such that the plaintiff could not make claim to full payment from just one party, then the payment by one of the parties for the obligations of another would prevent a claim for contribution.

But Indiana does not follow the classical approach; *Whiteman* changed that. In *Whiteman*, the Indiana Supreme Court adopted the approach now embodied in the Restatement (Third) of Restitution & Unjust Enrichment, specifically §§ 5 and 6 cmt. e. Later in the Restatement–section 23 to be precise–gives us a peak into how contribution works under the *Whiteman*approach. Before looking at the answer, let us first look back to *New v. T3 Investments Corp.* to see what contribution is:

> "The 'doctrine of contribution rests on the principle that where parties stand in equal right, equality of burden becomes equity.'" "Moreover, the right of contribution is based upon 'natural Justice, [and] it applies to any relation, including that of joint contractors, where equity

> between the parties is equality of burden, and one of them discharges more than his share of the common obligation.'" "The right of contribution operates to make sure those who assume a common burden carry it in equal portions." "[E]xcept as provided in I.C. 26-1-3.1-419(e) or by agreement of the affected parties, a party having joint and several liability who pays the instrument is entitled to receive from any party having the same joint and several liability contribution in accordance with applicable law."

Basically, if after full reflection of all the equities of the situation, a reasonable person would say "that ain't right" when considering whether one party should be stuck paying for everything, then the one that paid will be able to claim a portion of repayment from the other. Of course it is more complicated than that, but not much.

Let us now turn to Section 23 of the Restatement (Third) of Restitution & Unjust Enrichment:

> <u>§ 23 Performance of a Joint Obligation (Indemnity and Contribution)</u>
>
> (1) If the claimant renders to a third person a performance for which claimant and defendant are jointly and severally liable, the claimant is entitled to restitution from the defendant as necessary to prevent unjust enrichment.
>
> (2) There is unjust enrichment in such a case to the extent that
>
> (a) the effect of the claimant's intervention is to reduce an enforceable obligation of the defendant to the third person, and
>
> (b) as between the claimant and the defendant, the obligation discharged (or the part thereof for which the claimant seeks restitution) was primarily the responsibility of the defendant.

Notice that despite more than one hundred years separating the Third Restatement and *Briggs*, we get the same result if the parties are jointly liable. In *New v. T3 Investments Corp.*, "[t]he Guarantors each agreed to be jointly and severally liable for the full amount of [the] indebtedness under the Note[.]" The settlement agreement made no difference. Consequently, "under these circumstances," there is no question T3 could seek contribution.

But what then of where the Restatement and *Briggs* depart–where the parties are not jointly liable? If the settlement agreement had specified that the parties were individually liable only for their specific portion, then things would be

different. Under *Briggs*, T3 could not make a claim. Under the Restatement approach the outcome is different. The contract would have fixed any debate over how the liability was apportioned. Thus, there would be no "recognized uncertainty," merely an errant payment by T3 of more money than it owed. Either way, under *Whiteman*, T3 is getting repaid.

Mind you, the application of the voluntary payment doctrine has nothing to do with the release language in the settlement agreement. The doctrine exists outside of contractual obligations, and nothing is changing the fact that the settlement agreement did not release the guarantors from claims against each other.

Join us again next time for further discussion of developments in the law.

Sources

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