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# Reformation in Arkansas

Howard W Brill



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# REFORMATION IN ARKANSAS

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Reformation is an equitable remedy by which the court rewrites or reforms the written contract, or instrument, to correspond to the original and actual intent of the parties.<sup>1</sup> If the parties contract, but their agreement is mistakenly transcribed, then reformation is the appropriate remedy to correct the mistake in integration.

The long established remedy is based on the maxim that equity looks to the substance and not merely the form.<sup>2</sup> Reformation is not based on what the parties knew or didn't know at the time of the contract; reformation is based on what the parties intended in light of their knowledge, whether complete or incomplete, disputed or undisputed. Reformation requires a mistake, not in the agreement, but in putting the agreement, however faulty or unwise it may have been, on paper.

Reformation is restitutionary in nature in that it prevents the defendant from being unjustly

enriched<sup>3</sup> by a mistake in the transcription of the agreement. But the remedy is also declaratory in that it clarifies the status of the parties under the writing before an actual dispute manifests itself. In this sense, it is a form of the ancient "*bill quia timet*," a preventive action brought "because he fears."

Reformation is sometimes described as an extraordinary remedy which courts should exercise with great caution. The reason for such restraints is clear: written instruments should not be modified or altered based on oral testimony without certain proof.<sup>4</sup>

## A. Requirements

For reformation to be available, the parties must have arrived at a complete agreement,<sup>5</sup> not merely a tentative agreement, a plan for negotiations, or a suggestion.<sup>6</sup> Reformation is not avail-

1 Roberson Enterprises, Inc. v. Miller Land and Lumber Co., 287 Ark. 422, 700 S.W.2d 57 (1985); Kohn v. Pearson, 282 Ark. 418, 670 S.W.2d 795 (1984).

2 Howard W. Brill, *The Maxims of Equity*, 1993 ARK. L. NOTES 29, 33. Reformation is also said to rest on the maxim that equity treats as done that which ought to be done. Johnston v. Sorrels, 21 Ark. App. 87, 729 S.W.2d 21 (1987).

3 See generally, HOWARD W. BRILL, ARKANSAS LAW OF DAMAGES (3rd ed. 1996) § 31-2.

4 Mutual of Omaha Ins. Co. v. Russell, 402 F.2d 339 (10th Cir. 1968).

5 Lambert v. Quinn, 32 Ark. App. 184, 798 S.W.2d 448 (1990).

6 See Delone v. United States Fid. & Guar., 17 Ark. App. 229, 707 S.W.2d 329 (1986).

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able when the parties had an agreement but never put it in writing. A mere promise to put the terms in writing cannot be a basis for reformation.<sup>7</sup> Nor is reformation available when the parties had an agreement, but intentionally left the written agreement incomplete as to details. Likewise, reformation is not available to correct an ambiguous term in the written agreement when the parties had no mutual understanding as to the term.<sup>8</sup>

Insurance contracts are a frequent source of reformation litigation. The insured assumes he is covered for a particular occurrence, but after the loss occurs is informed by the company that the written policy does not cover that risk. The insured's typical statement will be "I told my insurance agent I needed coverage for this risk, and he assured me it was in the policy." The defense may be that the insurance agent lacked the authority to enter into the contract or the home office did not even offer the policy that the insured expected. In other instances the insured and the agent may have different recollections as to what was said and what was intended.

Despite the potential swearing match,<sup>9</sup> reformation is not uncommon in such situations.

For example, a court will reform an insurance policy that omitted, by mistake, a vehicle that the insured and the insurer intended to include,<sup>10</sup> or a policy issued for less than the agreed upon coverage.<sup>11</sup> Similarly, a worker's compensation insurance policy may be reformed to include a deceased member of the partnership.<sup>12</sup> Likewise, in real property instruments, a court will reform a deed that conveys all interests to the grantee when the parties intended to exclude mineral rights from the transfer,<sup>13</sup> will reform a note to include an omitted provision,<sup>14</sup> and will reform the property description in a mortgage to include the parcel on which the improvements were located.<sup>15</sup> The payments prescribed in a promissory note may be reformed when the payments were calculated on an erroneous interest rate.<sup>16</sup>

Reformation will work in either direction—to expand the terms or conditions of the written agreement to correspond to the prior oral agreement, or to limit or restrict the written terms. For example, equity will reform a note and mortgage that mistakenly excluded a 29 acre tract,<sup>17</sup> and likewise will reform a deed that mistakenly

7 *Id.*

8 *See* Peacock v. Bryant, 269 Ark. 658, 600 S.W.2d 413 (Ark. App. 1980) (no evidence of fraud, trickery, or inequitable conduct).

9 *See* Sims v. Wilson, 255 Ark. 465, 501 S.W.2d 214 (1973).

10 *Equity General Agents Inc. v. O'Neal*, 15 Ark. App. 302, 692 S.W.2d 789 (1985) (pickup truck excluded).

11 *Granite State Ins. Co. v. Bacon*, 266 Ark. 842, 586 S.W.2d 254 (1979) (insurance agent erroneously typed a lesser amount of coverage than requested; reformation granted); *General Agents Ins. Co. v. St. Paul Ins. Co.*, 22 Ark App. 46, 732 S.W.2d 868 (1987) (renewal of insurance policy did not provide same coverage; reformation granted because of insurer's mistake). *Compare* *American Mut. Liab. Ins. Co. v. Rockwood Ins. Co.*, 271 Ark. 167, 608 S.W.2d 24 (Ark. App. 1980) (no decisive evidence to support allegation that parties intended the addition of a multiplier factor to increase insurance premiums).

12 *American Casualty Co. v. Hambleton*, 233 Ark. 942, 349 S.W.2d 644 (1961).

13 *Falls v. Utley*, 281 Ark. 481, 665 S.W.2d 862 (1984); *Turner v. Pennington*, 7 Ark. App. 205, 646 S.W.2d 28 (1983) (only surface rights intended). *See also* *Hope v. Hope*, 333 Ark. 324, \_\_\_ S.W. 2d \_\_\_ (1998) (timber deed reformed and limited to authority to harvest timber growing as of specified date).

14 *Morton v. Park View Apartments*, 315 Ark. 400, 868 S.W.2d 448 (1993) (note reformed to include a no recourse provision omitted because of mutual mistake).

15 *Bell v. Mid-State Homes, Inc.*, 248 Ark. 600, 453 S.W.2d 57 (1970).

16 *Yeargan v. Bank of Montgomery County*, 268 Ark. 752, 595 S.W.2d 704 (1980) (payments calculated on 4% instead of 8%).

17 *Johnston v. Sorrels*, 21 Ark. App. 87, 729 S.W.2d 21 (1987).

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included a parcel of land not intended by the parties.<sup>18</sup> Equity will reform a guaranty agreement that contains the wrong debt in the instrument<sup>19</sup> and an employment agreement with a single year provision instead of the negotiated two year provision.<sup>20</sup> Equity can reform multiple documents that come from a single transaction.<sup>21</sup>

Sometimes what appears to be a mistake is simply the result of a calculated gamble. Both parties negotiated in the dark, assumed a certain risk, or guessed as to the future events. Hindsight as to what would have been a better bargaining position will not support reformation.<sup>22</sup>

Reformation is not a remedy that permits a court to rewrite an instrument to make it fair or reasonable or convenient or wise.<sup>23</sup> For example, when the conveyance of land included access that turned out to be inadequate, the chancellor had no authority to reform the deed and place access in a different location. If the parties were fundamentally mistaken in making the contract, the remedy, if any, is rescission, not reformation. If the parties believed that Blackacre had an adequate supply of water and was thereby sold for \$25,000, but if in reality Blackacre lacked water, the buyer has no basis for reformation. Since the underlying agreement was based on a mutual mis-

take, the appropriate remedy is to rescind the contract and restore the parties to their prior status.

### B. Jurisdiction and Procedure

As an equitable remedy, reformation falls within the exclusive subject matter jurisdiction of the chancery court.<sup>24</sup> It is asserted as a primary claim, that is, as a *bill quia timet*, to give the plaintiff relief from a potential or threatened dispute. Likewise, the claim may be accompanied by a prayer for damages for breach of the reformed contract. An action seeking reformation that is filed in circuit court must be transferred to chancery court.<sup>25</sup>

However, in light of the underlying purpose of equity courts,<sup>26</sup> the presence of an adequate remedy at law bars equity involvement and equitable relief. For example, concluding that a decree of reformation "would be a vain and useless act," a chancellor denied relief because the party would achieve the same result in reality by prevailing on a counterclaim pending in circuit court.<sup>27</sup>

Additionally, the remedy of reformation may be sought in a variety of procedural contexts. A complaint seeking damages for breach of contract may be answered with a counterclaim for refor-

18 *Lambert v. Quinn*, 32 Ark. App. 184, 798 S.W.2d 448 (1990) (parties understood that .42 acres were not to be transferred). See *Anderson v. Welborn*, 254 Ark. 280, 492 S.W.2d 892 (1973) (reformation of property description in deed).

19 *Akin v. First National Bank of Conway*, 25 Ark. App. 341, 758 S.W.2d 14 (1988).

20 *Hampton School District v. Phillips*, 251 Ark. 90, 470 S.W.2d 934 (1971).

21 *Riddick v. Streett*, 313 Ark. 706, 858 S.W.2d 62 (1993) (the lots in an entire subdivision).

22 See *Printing Industries Association of Northern Ohio, Inc. v. Graphic Arts International Union, Local No. 546*, 628 F. Supp. 1103 (N.D. Ohio 1985) (parties assumed the risk as to which cost of living index to use).

23 See *Bonner v. Sikes*, 20 Ark. App. 209, 727 S.W.2d 144 (1987) (error to reform a deed to grant access to the tract in a more convenient or appropriate location than intended by the parties).

24 *Hampton School District v. Phillips*, 251 Ark. 90, 470 S.W.2d 934 (1971). An action to reform is an action on a contract and is governed by the general venue statute. *Shelter Mutual Ins. Co. v. Taylor*, 281 Ark. 60, 661 S.W.2d 369 (1983). See ACA § 16-60-116(a). See John J. Watkins, *A Guide to Arkansas Venue*, 1995 ARK. L. NOTES 83.

25 See *Arbor Acres Farm, Inc. v. Benedict*, 278 Ark. 14, 642 S.W.2d 893 (1982).

26 See Howard W. Brill, *Law and Equity in Arkansas: Will Liles v. Liles Lead Us Out of the Morass?*, 1987 ARK. L. NOTES 1.

27 See *Arbor Acres Farm, Inc. v. Benedict*, 278 Ark. 14, 642 S.W.2d 893 (1982).

mation. Suppose the plaintiff alleges breach of contract and sues for \$100,000 damages in circuit court. The defendant responds that the written contract mistakenly integrated the oral agreement, and that the amount claimed should not have been \$100,000, but only the lesser amount upon which the parties had agreed. Upon raising this equitable defense, the defendant should move to transfer the entire action to a court of equity.<sup>28</sup> Although the circuit judge does have authority to sever an action, retaining part and transferring the remainder,<sup>29</sup> in this instance the unity of the action and the close relationship of the complaint and the equitable defense should persuade the court to transfer the entire action to a court of equity. Equity, under the clean up power,<sup>30</sup> would have authority to award damages, in addition to or instead of equitable relief. However, this analysis and conclusion is undermined if the plaintiff demanded a jury trial. Recent authority suggests that the right to the jury trial may bar transfer of the entire claim.<sup>31</sup> Even if only part of the action were transferred, the chancellor might enjoin the plaintiff from proceeding with the claim for damages until the issue of reformation is resolved.

The reformation of a contract recreates the intended contract from the date of original execution.<sup>32</sup> Following reformation, the chancery court may, if appropriate, award damages for the breach.<sup>33</sup>

In a reformation suit, all the parties to the contract are necessary parties.<sup>34</sup> However, reformation is not limited to those who were parties to the mistake. For example, the buyer at a foreclosure sale may seek reformation of the commissioner's deed even though the mistaken property description initially arose between the mortgagor and the mortgagee.<sup>35</sup> The buyer must establish that he expected to purchase land that was not covered within the property description. The factual issue as to each subsequent party is whether the party intended to purchase the land as described or expected to purchase land that was in reality not included within the actual property description.<sup>36</sup> In the former instance, reformation is not available; in the latter, it is. However, a non party lacking a clear interest may not seek reformation.<sup>37</sup>

In some instances reformation may be sought against individuals who were not parties to the

28 ACA § 16-57-104(c)(2).

29 See *Equity General Agents, Inc. v. O'Neal*, 15 Ark. App. 302, 692 S.W.2d 789 (1985) (circuit court severed the reformation count and transferred to chancery).

30 BRILL, *supra* note 3, § 2-3.

31 See *Walker v. First Commercial Bank, N.A.*, 317 Ark. 617, 880 S.W.2d 316 (1994).

32 *Hampton School District v. Phillips*, 251 Ark. 90, 470 S.W.2d 934 (1971).

33 *Id.*

34 See *Riddick v. Streett*, 313 Ark. 706, 858 S.W.2d 62 (1993) (all grantors or heirs are necessary for reformation of a deed); *Harbour v. Sheffield*, 269 Ark. 932, 601 S.W.2d 595 (Ark. App. 1980) (grantors are necessary parties). Deeds to separate parties may be reformed when both grantees took from a common grantor. *Galyen v. Gillenwater*, 247 Ark. 701, 447 S.W.2d 137 (1969).

35 *Johnston v. Sorrels*, 21 Ark. App. 87, 729 S.W.2d 21 (1987) (29 acre tract excluded from description). See also *Commonwealth Building & Loan Association v. Wingo*, 189 Ark. 1033, 75 S.W.2d 1008 (1934) (reformation of release deed). A party who purchases land from the state at a tax sale but acquires a defective title is not entitled to have it reformed because the state itself had acquired no title to the property. However, the buyer may have his money refunded on a rescission theory. See *Undernehr v. Sandlin*, 35 Ark. App. 207, 816 S.W.2d 635 (1991).

36 *Johnston v. Sorrels*, 21 Ark. App. 87, 729 S.W.2d 21 (1987).

37 See *Nichols v. Wray*, 325 Ark. 326, 925 S.W.2d 785 (1996) (sister not permitted to seek reformation of a certificate of deposit in the name of other sister and deceased mother).

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original contract. For example, if the mistake is in favor of the mortgagor by omitting property from the description, the mortgagee may seek reformation against the mortgagor or any subsequent purchaser with notice of the mistake.<sup>38</sup> Likewise a subsequent mortgagee may seek reformation.<sup>39</sup> However, reformation will not be granted against bona fide purchasers or encumbrancers for value and without notice.

Occasionally, a decree of reformation may do more than simply change language. In an instance when the court found that the warranty deed was not intended to be a conveyance of clear title, it interpreted the deed as vesting title in the defendants, not as grantees, but as the trustees of an express trust for the purpose of cultivating the land during the life of the grantor, with the title to property subsequently reverting to the heirs of the grantor.<sup>40</sup>

Sometimes the term reformation is broadly or mistakenly used to cover other remedies. For example, the trial court "reformed" a contract by reducing the price of land by \$25,000 to compensate for the cost of moving a water line in light of the seller's misrepresentation.<sup>41</sup> The appropriate

remedy would be abatement, by which the court adjusts the purchase price to correspond to the difference between what the parties intended and what was included. If the parties intended to convey "640 acres, more or less," but only 355 acres are actually conveyed, the buyer may seek an abatement of the price.<sup>42</sup> Reformation corrects a mistake in putting the agreement in writing; abatement, like rescission of the contract, corrects a mistake arising out of the original agreement. Abatement in real estate transactions is not appropriate if the land was sold by the tract or by the gross,<sup>43</sup> if the discrepancy was insubstantial,<sup>44</sup> or if the court concludes that the buyer had a duty to survey the land prior to conveyance.<sup>45</sup>

### C. Evidence

Reformation must be supported by clear and convincing evidence<sup>46</sup> in two respects.<sup>47</sup> First, the evidence must demonstrate the actual intent of the parties. Without that, the written instrument cannot be reformed or rewritten. The passage of time, the absence of witnesses to the oral agreement, or the death of the parties may make it dif-

38 Craig v. Pendleton, 89 Ark. 259, 116 S.W. 209 (1909).

39 Bell v. Mid-State Homes, Inc., 248 Ark. 600, 453 S.W.2d 57 (1970) (all parties intended to mortgage the property upon which the house was located).

40 Arnett v. Lillard, 245 Ark. 939, 436 S.W.2d 106 (1969).

41 Christy Co. v. Ainbinder/Searcy Ltd., 3 Ark. App. 63, 621 S.W.2d 886 (1981).

42 See Williams v. J.W. Black Lumber Co., 275 Ark. 144, 628 S.W.2d 13 (1982). Abatement, if granted, typically results in a reduction of the purchase price and a refund in effect to the buyer. Suppose the buyer received 20% more land than the parties expected to convey? Will abatement work to compel the buyer to pay more for the land actually received? The court may offer the buyer an option: agree to pay more or have the entire contract rescinded because of mutual mistake and then renegotiate based on the correct information. See DAN B. DOBBS, REMEDIES (1973) §§ 11.3, 12.13.

43 Young v. Bradshaw, 224 Ark. 467, 274 S.W.2d 466 (1955) (shortage of 36%; no relief); Gilbertson v. Clark, 175 Ark. 1118, 1 S.W.2d 823 (1928) (shortage of 25%; no relief).

44 Birch-Brook, Inc. v. Ragland, 253 Ark. 161, 485 S.W.2d 225 (1972) (parties relied on a survey that indicated "89.293 acres, more or less"; tract actually had 81.55 acres; parties never agreed to a sale by the acre; no reformation or abatement).

45 See Howard W. Brill, *Specific Performance in Arkansas*, 1995 ARK. L. NOTES 17, 23. Abatement may be sought to compensate for any deficiency in quantity, quality, title or other matters affecting the property.

46 Falls v. Utley, 281 Ark. 481, 665 S.W.2d 862 (1984); Mizell v. Carter, 255 Ark. 960, 504 S.W.2d 743 (1974). See Sims v. Wilson, 255 Ark. 465, 501 S.W.2d 214 ("clear, cogent and convincing evidence" required).

47 See Christy Co. v. Ainbinder/Searcy Ltd., 3 Ark. App. 63, 621 S.W.2d 886 (1981) ("clear, convincing and decisive").

ficult or impossible to demonstrate the original intent by clear and convincing evidence.<sup>48</sup> Second, the same degree of evidence must demonstrate the grounds for reformation.<sup>49</sup> However, the proof need not be undisputed.<sup>50</sup> In another context, clear and convincing evidence has been defined as "evidence by a credible witness whose memory of the facts about which he testifies is distinct, whose narration of the details is exact and in due order, and whose testimony is so direct, weighty, and convincing as to enable the fact-finder to come to a clear conviction, without hesitation, of the truth of the facts related."<sup>51</sup>

Admittedly some cases also indicate that the proof "must establish the right beyond a reasonable doubt,"<sup>52</sup> but that language is superfluous and misleading verbiage because some of the same cases say "the only requirement is that there be more than a mere preponderance."<sup>53</sup> The limitation of a higher evidentiary standard is necessary to ensure that equity does not create an agreement where none previously existed. Although the cases may adopt slightly varying evidentiary stan-

dards as to the quantum, all variations are in agreement that something more than a mere preponderance of the evidence is required.

The role of the appellate court is to inquire whether the chancellor's finding of clear and convincing evidence to support reformation was clearly erroneous.<sup>54</sup> Although deferring to the superior position of the chancellor to evaluate the evidence,<sup>55</sup> an appellate court reviews equity cases *de novo* and will enter a decree of reformation when it should have been entered by the trial chancellor.<sup>56</sup> However, on occasions it will defer to the chancellor's position as a fact finder and remand for further proceedings.<sup>57</sup> The appellate court will also reverse the trial court's grant of reformation if the decree is not supported by satisfactory evidence.<sup>58</sup>

The parole evidence rule bars the admission in evidence of contemporaneous or prior oral agreements that would contradict or alter the terms of a written contract.<sup>59</sup> But parole evidence is admissible to show mutual mistake<sup>60</sup> or fraud,<sup>61</sup> and to establish the true intentions of the parties in a

48 See *Dobbins v. Hayden*, 280 Ark. 523, 659 S.W.2d 946 (1983).

49 See *Morton v. Park View Apartments*, 315 Ark. 400, 868 S.W.2d 448 (1993); *Continental Cas. Co. v. Didier*, 301 Ark. 159, 783 S.W.2d 29 (1990).

50 *Hope v. Hope*, 333 Ark. 324, \_\_\_ S.W. 2d \_\_\_ (1998); *Kohn v. Pearson*, 282 Ark. 418, 670 S.W.2d 795 (1984); *Winkle v. Grand National Bank*, 267 Ark. 123, 601 S.W.2d 559 (1980); *Bicknell v. Barnes*, 255 Ark. 697, 501 S.W.2d 761 (1973); *Turner v. Pennington*, 7 Ark. App. 205, 646 S.W.2d 28 (1983).

51 *Bishop v. Bishop*, 60 Ark. App. 164, 169, 961 S.W.2d 770 (1998)(proof to uphold an inter vivos gift).

52 See *Merriman v. Yuterman*, 291 Ark. 207, 723 S.W.2d 823 (1987).

53 See *Gastineau v. Crow*, 222 Ark. 749, 262 S.W.2d 654 (1953).

54 *Akin v. First National Bank of Conway*, 25 Ark. App. 341, 758 S.W.2d 14 (1988). See ARK. R. CIV. PRO. 52(a).

55 *Jones v. Jones*, 27 Ark. App. 297, 770 S.W.2d 174 (1989); *Akin v. First National Bank of Conway*, 25 Ark. App. 341, 758 S.W.2d 14 (1988).

56 See *Hope v. Hope*, 333 Ark. 324, \_\_\_ S.W.2d \_\_\_ (1998). See also *Equity General Agents, Inc. v. O'Neal*, 15 Ark. App. 302, 692 S.W.2d 789 (1985).

57 For example, *Johnston v. Soirels*, 21 Ark. App. 87, 729 S.W.2d 21 (1987) (appellate court reversed refusal to decree reformation, but remanded for further action).

58 *Dobbins v. Hayden*, 280 Ark. 523, 659 S.W.2d 946 (1983).

59 See *Sellers v. West-Ark Const. Co.*, 283 Ark. 341, 676 S.W.2d 726 (1984); *Gainer v. Tucker*, 255 Ark. 645, 502 S.W.2d 636 (1973).

60 *Morton v. Park View Apartments*, 315 Ark. 400, 868 S.W.2d 448 (1993).

61 *Garot v. Hopkins & Coates*, 266 Ark. 243, 583 S.W.2d 54 (1979).

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reformation action.<sup>62</sup> The parol evidence must be "clear, decisive and unequivocal,"<sup>63</sup> but it need not be undisputed.<sup>64</sup> For example, nothing prohibits a chancellor from granting reformation even if the only witnesses are the two parties to the contract who are in sharp disagreement as to the actual intent.<sup>65</sup>

The statute of frauds<sup>66</sup> requires that certain contracts be in writing and evidenced by a memorandum.<sup>67</sup> The memorandum must be sufficient to satisfy the statute and thus make the contract enforceable in law and equity. Without any writing, reformation is not available, though rescission or another restitutionary remedy might be.<sup>68</sup> With a writing that satisfies the general requirements of the statute of frauds, reformation is available to correct mistakes in transcription. Reformation might also be available if by mistake crucial details were omitted from the memorandum, though the writing itself still satisfied the statutory requirement.

However, if the parties intentionally omitted a term from the memorandum, reformation is unavailable to correct the omission because the written agreement corresponds to the intent of the parties. Even with a writing that satisfies the memorandum requirement of the statute of

frauds, reformation is not necessarily available. For example, clear and convincing evidence may not elevate the oral agreement over the terms of the written agreement. Because reformation is intended to prevent unjust enrichment, neither the statute of frauds nor the parol evidence rule should be employed or interpreted to bar this result.<sup>69</sup>

### D. Mistake

The customary basis for reformation is mutual mistake. A mistake is a state of mind not in accord with the facts.<sup>70</sup> Mistake does not exist if the parties were unconcerned or manifested conscious indifference to the specific facts at the time of the agreement.<sup>71</sup> The mistake must be basic and a mistake of fact. A mutual mistake is one shared by both parties at the time the agreement is incorporated in written form.<sup>72</sup> Both parties must have accepted the written instrument under the same misconception with regard to the terms of the written instrument.<sup>73</sup> Whether mutual mistake occurred is a question of fact.<sup>74</sup>

A mistake as to the existing condition or facts at the formation of the contract will not support reformation, but may support cancellation or

62 *Galyen v. Gillenwater*, 247 Ark. 701, 447 S.W.2d 137 (1969) (reformation of boundary lines in deeds from a common grantor).

63 *Falls v. Utley*, 281 Ark. 481, 665 S.W.2d 862 (1984).

64 *Beneaux v. Sparks*, 144 Ark. 23, 221 S.W. 465 (1920).

65 See, e.g., *Falls v. Utley*, 281 Ark. 481, 665 S.W.2d 862 (1984).

66 ARK. CODE ANN. § 4-59-101(a).

67 BRILL, *supra* note 3, § 17-2.

68 BRILL, *supra* note 3, § 31-2, 3.

69 See DOBBS, *supra* note 42, §§ 9.5, 11.6.

70 *Continental Cas. Co. v. Didier*, 301 Ark. 159, 783 S.W.2d 29 (1990). See DOBBS, *supra* note 42, § 11.2.

71 *Williams v. Killins*, 256 Ark. 491, 508 S.W.2d 753 (1974) (parties were unconcerned about the exact location of the boundary line).

72 *Delone v. United State Fid. & Guar. Co.*, 17 Ark. App. 229, 707 S.W.2d 329 (1986).

73 *Lambert v. Quinn*, 32 Ark. App. 184, 798 S.W.2d 448 (1990); *Yeargan v. Bank of Montgomery County*, 268 Ark. 752, 595 S.W.2d 704 (1980).

74 *Lambert v. Quinn*, 32 Ark. App. 184, 798 S.W.2d 448 (1990).



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rescission. If the mutual mistake occurred in the original agreement, the remedy is rescission.<sup>75</sup> The court cannot reform a clause or phrase as to which the parties were fundamentally mistaken. To use the classic example, if the parties negotiated the purchase of a barren cow, the court cannot reform the purchase price when later developments revealed that they were mistaken as to her fertility status.<sup>76</sup> How can the court possibly know the value that a willing buyer and seller would have put on this particular cow? On the other hand, if the mistake occurred in the transcription of the original agreement, the remedy is reformation. If the agreement was for \$100, but the written contract was \$200, the court can reform. The facts dictate the remedies; the plaintiff does not have a choice.

Reformation may be granted regardless of whether the mistake was made by one of the parties,<sup>77</sup> an employee of a party,<sup>78</sup> or an independent scrivener.<sup>79</sup> The mistake of a bank employee in typing a name on a certificate of deposit can be reformed to indicate the name of the correct payee.<sup>80</sup> Even though the mistake was made by a non-party and might arguably be viewed as unilateral, the courts do not hesitate in granting reformation, properly so in that both parties, individually and mutually, believed the written instrument incorporated their agreement and thus

accepted the instrument.<sup>81</sup>

What about a mistake in the legal effect of the language? Suppose the parties expected that the conveyance would reserve a life estate to the grantor, but the language chosen did not authorize it. If they had a clear agreement, then the language in the conveyance could be reformed. If the life estate was not part of the antecedent oral agreement, then reformation is not appropriate.

Black letter law holds that if only the party seeking reformation was mistaken, the mistake is unilateral, in which case reformation is granted only if the other party engaged in fraud or some inequitable conduct.<sup>82</sup> For example, an insured sought reformation of a liability insurance policy arguing that the parties intended a "deluxe policy" and a "broad form" of protection, but that the actual policy provided no coverage for claims arising from the sale of alcohol to minors. In denying reformation, the court found that the insured did not believe he had been insured against risks arising from the illegal sale of liquor; accordingly he was not mistaken. Further, an experienced policy holder would have investigated the coverage upon receiving the original policy, and nothing suggested any inequitable conduct on the part of the insurer.<sup>83</sup>

Similarly, a misunderstanding between the insured and the agent for the insurer as to the

75 For example, *Carter v. Matthews*, 288 Ark. 37, 701 S.W.2d 374 (1986) (both parties mistaken as to whether land was suitable pasture for horses); *Glasgow v. Greenfield*, 9 Ark. App. 224, 657 S.W.2d 578 (1983) (contract rescinded because of clear and convincing evidence that both parties believed that the buyer would be able to obtain a state liquor license).

76 See *Sherwood v. Walker*, 66 Mich. 568, 33 N.W. 919 (1887).

77 *Hope v. Hope*, 333 Ark. 324, \_\_\_ S.W.2d \_\_\_ (1998) (mistake by grantor of deed); *Yeargan v. Bank of Montgomery County*, 268 Ark. 752, 595 S.W.2d 704 (1980) (mistake by party to contract).

78 *Winkle v. Grand National Bank*, 267 Ark. 123, 601 S.W.2d 559 (1980); *Pennsylvania Millers Mutual Ins. Co. v. Walton*, 236 Ark. 336, 365 S.W.2d 859 (1963) (both insurance agent and insured believed that policy covered water escape damage; reformation granted).

79 See *Akin v. First National Bank of Conway*, 25 Ark. App. 341, 758 S.W.2d 14 (1988).

80 *Jones v. Jones*, 27 Ark. App. 297, 770 S.W.2d 174 (1989).

81 See *Kohn v. Pearson*, 282 Ark. 418, 670 S.W.2d 795 (1984).

82 *Delone v. United States Fid. & Guar.*, 17 Ark. App. 229, 707 S.W.2d 329 (1986). See also the dissenting opinion of Justice Newbern in *Morton v. Park View Apartments*, 315 Ark. 400, 408, 868 S.W.2d 448 (1993).

83 *Continental Cas. Co. v. Didier*, 301 Ark. 159, 783 S.W.2d 29 (1990) (insurance agent did not act inequitably in failing to explain that policy did not cover illegal sale of liquor to minor).

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amount of the policy limits desired did not, by itself, support reformation against the insurance company.<sup>84</sup> Likewise, a party to a contract contended that the first payment was due July 1, although the written contract set a June 15th date. Since the other party was never in doubt as to the June 15th time for payment, any mistake was only unilateral.<sup>85</sup>

However, simply describing the mistake as unilateral does not bar an action for reformation. Consider an individual who negotiates with an insurance company for a policy obligating it to pay \$500 a year. If, by mistake, the insurance company issues a policy calling for \$500 a month, its mistake is entirely its fault. However, reformation will be granted.<sup>86</sup> Rather than focus on the clerical error in issuing the policy, the mistake is more appropriately described as mutual in that both parties believed that the written instrument was correct. In the absence of other factors, such as a delay in seeking reformation after discovery of the mistake or reliance by the insured on the terms of the written policy, reformation is appropriate.

Unilateral mistake combined with some form of inequitable conduct may support reformation as an alternative to rescission. Consider the purchase of a mobile home. The seller contacted the finance company holding the note and learned that the payoff amount was \$8800. The contract with the buyer therefore provided for "\$8800 in monthly installments of \$130." But the \$8800 represented the cash payoff, and not the principal and interest to be paid in monthly payments. After the buyer had paid \$8800 and requested a deed, the seller sought reformation to provide for \$130 a month "until the balance was paid off." The mistake of the seller in equating the amount

to immediately pay off the existing loan with the amount to be paid periodically after assumption of the loan by the buyer was unilateral. Since the buyer had not engaged in any inequitable conduct, reformation was not appropriate.<sup>87</sup> However, suppose the buyer had recognized the mistake in the terms of the written contract for the purchase of the mobile home and had remained silent. The court would be justified in concluding that the silence amounted to inequitable conduct and in granting reformation in favor of the seller.

The presence of fraud further simplifies the judicial task. Consider the situation in which the parties reach an agreement but one party is dissatisfied and changes the terms in the written instrument. Even if the innocent party fails to read the instrument before signing, reformation is available against the party who was guilty of outright fraud.

Reformation may be appropriate when the written document contains terms that are illegal or unenforceable. For example, the court reformed a promissory note and reduced a usurious interest rate to 10%. The parties were not mutually mistaken, but the court concluded that the borrower's conduct in inserting the rate tainted of misrepresentation, and thus the note should be reformed to make it enforceable.<sup>88</sup> However, the criticism with reformation in such a situation is that the court is writing a new agreement.

If, in contrast, one party mistakenly proposed terms for the contract, which the other party innocently accepted, reformation is not available because no discrepancy exists between the agreement and the written instrument. The classic scenario is the contractor who submits a bid on a project and, as the lowest bidder, is awarded and signs the contract. Subsequently, the contractor

84 *Delone v. United States Fid. & Guar.*, 17 Ark. App. 229, 707 S.W.2d 329 (1986) (agent misunderstood intent of insured and reduced coverage from \$500,000 to \$250,000; no reformation against insurance company).

85 *Westlund v. Melson*, 7 Ark. App. 268, 647 S.W.2d 488 (1983).

86 *See Travelers Ins. Co. v. Bailey*, 124 Vt. 114, 197 A.2d 813 (1964).

87 *Wright v. Langdon*, 274 Ark. 258, 623 S.W.2d 823 (1981).

88 *Turney v. Roberts*, 255 Ark. 503, 501 S.W.2d 601 (1973).

discovers a mathematical, clerical or even judgment error in the calculation of the bid. The corrected bid, with the undoubtedly higher amount, cannot be forced on the other party through the mechanism of reformation. The issue then is whether such a unilateral mistake will support rescission of the agreement by the mistaken party. Contracts may be rescinded for a unilateral mistake, provided (1) the mistake was so substantial that to enforce the contract would be unconscionable; (2) the mistake relates to a material feature of the contract; (3) the mistake occurred despite the exercise of reasonable care by the mistaken party; and (4) rescission of the contract will not cause serious prejudice to the other party, except for the loss of its bargain. Upon such a showing, equity has power to grant rescission of the contract and relieve the mistaken party from damages.<sup>89</sup>

### E. Defenses and Delay

The affirmative defense of laches will bar the reformation remedy. Laches has two elements: unreasonable delay by the plaintiff in seeking remedy, and resulting harm to the defendant.<sup>90</sup> The mere passage of time is not sufficient to invoke the defense. For example, the passage of

two years,<sup>91</sup> eleven years,<sup>92</sup> or even 67 years<sup>93</sup> did not bar reformation of a deed. Some decisions suggest that the party seeking reformation has a heavier burden when the passage of time is greater.<sup>94</sup> The crucial question is whether, upon discovering the basis for reformation, the plaintiff acted promptly. The failure to timely assert equitable defenses such as laches or estoppel constitutes a waiver of those defenses.<sup>95</sup>

With an insurance policy, a mistake in coverage typically will not be discovered until after a loss has occurred. Such delay does not, by itself, bar reformation of the policy after the loss.<sup>96</sup> Likewise, the mere failure of the insured to read the contract before signing<sup>97</sup> or to review an insurance policy when received<sup>98</sup> does not bar reformation, although the court may have some discretion if the insured demonstrated neglect in failure to discover the mistake earlier.<sup>99</sup>

Unclean hands will bar a party from reformation.<sup>100</sup> For example, the allegations of a party that a deed was intended to be merely a mortgage were undercut by his representations in a child support matter that he owned no property and his statements to governmental assistance agencies that he was merely a tenant.<sup>101</sup>

89 *Mountain Home School District v. T.M.J. Builders, Inc.*, 313 Ark. 661, 858 S.W.2d 74 (1993); *Ark. State Highway Comm. v. Ortinger*, 232 Ark. 35, 334 S.W.2d 694 (1960). See Jack East, III, *Unilateral Mistakes in Bids for Construction Contracts*, ARK. LAWYER (July 1991) 38.

90 See Brill, note 2, p. 37.

91 See *Falls v. Utley*, 281 Ark. 481, 665 S.W.2d 862 (1984).

92 See *Turner v. Pennington*, 7 Ark. App. 205, 646 S.W.2d 28 (1983).

93 *Kohn v. Pearson*, 282 Ark. 418, 670 S.W.2d 795 (1984).

94 See *Dobbins v. Hayden*, 280 Ark. 523, 659 S.W.2d 946 (1983) (47 years after original conveyance).

95 *Jones v. Jones*, 27 Ark. App. 297, 770 S.W.2d 174 (1989).

96 See *General Agents Ins. Co. v. St. Paul Ins. Co.*, 22 Ark. App. 46, 732 S.W.2d 868 (1987).

97 *Lambert v. Quinn*, 32 Ark. App. 184, 798 S.W.2d 448 (1990).

98 *American Casualty Co. v. Hambleton*, 233 Ark. 942, 349 S.W.2d 664 (1961).

99 See *General Agents Inc. Co. v. St. Paul Ins. Co.*, 22 Ark. App. 46, 732 S.W.2d 868 (1987).

100 See Brill, note 2, p. 34.

101 *Plain v. Ray*, 245 Ark. 310, 432 S.W.2d 13 (1968).

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### F. Discretion

In light of the general policy that no litigant has a right to equitable relief, the chancellor retains discretion to deny reformation. Reformation will not be granted when it would harm the rights of innocent third parties, such as bona fide purchasers and lien holders. Although reformation of an insurance policy may be granted against the issuing insurance company, it will not lie against the successor company that merely assumed the liabilities of the prior policies.<sup>102</sup> The successor company had purchased for value without any notice of the alleged oral representations made in connection with the issuance of the policy.

Likewise, reformation of a deed was refused when the grantee had conveyed the property under the questioned property description to a third party before the commencement of the equitable action.<sup>103</sup> The original grantor may have conveyed more property than the parties intended, and thus may have a cause of action against the original grantee (based upon mistake or fraud), but has no claim against the subsequent grantee who purchased for value without any knowledge. Being too late to reform, the original grantor is limited to a claim for damages against the original grantee.

However, a subsequent party who acquired the property or contractual interest with notice of the error cannot defeat reformation. A subsequent grantee took actual possession of a five acre tract based upon the location of fences. Though the legal description did not indicate the intended tract, the fences did, thus permitting reformation of the deed against the subsequent grantee.<sup>104</sup>

### G. Reformation of Gifts

#### 1. Action by Donor

A donor may assert unjust enrichment to correct a mistake, even if unilateral. If the check conveying the gift is mistakenly made out to the wrong individual, the donor may cancel the gift. If the donor intended to convey only a life interest in Blackacre, but conveyed absolute title, the conveyance may be reformed. The donee may defeat reformation by showing expenditures made in good faith reliance on the gift, but cannot successfully argue that a donor should be barred from asserting the unjust enrichment of the donee in the reformation action.<sup>105</sup>

#### 2. Action by Donee

As a general proposition, the purported donee has no standing or right to seek reformation of a gift intended in his favor. The donor is free to correct the error if he desires. A donee who expected to receive \$5000 but only received \$500 would be foolish to sue the donor.

However, the rule changes upon the death of the donor. Case law permits the intended donee to demonstrate that the donor would have corrected the mistake if he had lived. For example, a donee who expected to be listed as the payee on a certificate of deposit discovered after the death of the purchaser that another name was inserted on the certificate. The donee successfully convinced the court that a simple typing error of a bank employee had been the cause of the mistake.<sup>106</sup> Likewise, the court reformed the property description in a deed that had been delivered by

102 *Jeffers v. American Pioneer Life Ins. Co.*, 256 Ark. 332, 507 S.W.2d 713 (1974).

103 *See Davidson v. Davidson*, 42 Ark. 362 (1883).

104 *Colbert v. Gann*, 247 Ark. 976, 448 S.W.2d 649 (1970) (subsequent grantee took possession of tract intended by the original parties rather than the tract described in the deed; unable to defeat reformation).

105 GEORGE E. PALMER, *THE LAW OF RESTITUTION* (1978) § 18.2.

106 *Jones v. Jones*, 27 Ark. App. 297, 770 S.W.2d 174 (1989).

the grantor, but not recorded until after his death.<sup>107</sup>

The courts are not as inclined to grant a remedy if the mistake was contained in a testamentary document. Suppose the testator had told the attorney drafting the will to include a bequest of \$50,000 to the Red Cross, but by oversight the executed document left a mere \$500 to the charity. Even though the charity's malpractice cause of action against the attorney may be limited,<sup>108</sup> equity has not traditionally permitted reformation of a will or trust.<sup>109</sup>

### Conclusion

The remedy for mistake in the formation of a contract is rescission of the contract; the remedy for mistake in the performance of a contract is restitution, in whole or in part; the remedy for mistake in the integration of a contract is reformation. Putting aside the issues of the type of mistake, the presence of inequity, the degree of fault, the negligence of the petitioning party, the role of others in the transcription, the impact upon third parties—the nature of reformation is simple: the written documents and instruments should reflect the actual agreement of the parties. Equity's task is to accomplish that objective and prevent unjust enrichment.

107 *Simmons v. Buchanan*, 34 Ark. App. 1, 803 S.W.2d 950 (1991) (gift to sister).

108 See ARK. CODE ANN. § 16-22-310. See HOWARD W. BRILL, *ARKANSAS PROFESSIONAL AND JUDICIAL ETHICS* (4th ed. 1997), page 19.

109 See DOBBS, note 42, § 11.6; PALMER, *supra* note 105, § 20.1.