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Comment on 'Profits Derived from Breach of Contract or Restitution'

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Commentary on 'Profits Derived from Breach of Contract: Damages or Restitution'*

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There is little with which to disagree in Professor Waddams' paper on the categorisation of damage recoveries in the cases posited, viz, those involving a breach which results in benefit to the breaching party but no loss of any consequence to the nonbreaching party. If the goal of contract remedies is to compensate the plaintiff for loss, then, presumably, there should be no recovery at all in such cases. At most there might be nominal damages to compensate for some transaction costs or perhaps as a 'declaration of rights'. In some of the cases considered by Waddams, breach might be considered to be useful as a means to promote efficiency by moving the breaching party's performance to a higher valuing user.

Waddams intuits, as many might, that refusing a remedy against a party who intentionally breaks a contract for personal or corporate gain could offend the general population of traders. The usual expectations among repeat players in a market will tend to inhibit those players from most contract breaches, but, even so, they may expect the law to give some strong public signal that breaches are disfavoured. The doctrine of efficient breach and the general common law rules limiting liability for contract defaults are not consistent with these expectations. The development of the common law limitations on contract recoveries and the justifications for the doctrine of efficient breach have been well covered by many different commentators. Waddams raises the interesting question whether restitution, as a separate body of law, might provide a basis for asserting a claim in a relatively small number of cases that come close to unjust enrichment and in which the plaintiff might not otherwise have a remedy.

The basis for an argument in support of some form of restitution-like recovery lies in the basic compensatory damage formula for contract breaches. In contract 'loss' generally refers to the failed expectancy — the measure of the disappointment for non-performance. The trier of fact must reconstruct a hypothetical future from evidence adduced about past behaviour and statements. If there is a writing, the terms of that writing impose additional specific constraints on the trier of fact. When the breach amounts to something as simple as a failure to deliver a promised chattel or service, the task is fairly simple. The plaintiff gets the difference in cost between the contract price and the cost of a substitute, or, in a few instances, the plaintiff may get the chattel itself.

Another kind of compensation case discussed by Waddams also seems simple. The contract calls for the provision of a service, such as fire protection,

* Commentary on 'Profits Derived from Breach of Contract: Damages or Restitution', a paper presented by Professor S Waddams at the Seventh Annual *JCL* Conference, Cambridge, September 1996 and appearing in this issue of the *Journal* at 115.

over a period of time. The service is not provided in breach of the contract, but there is no fire and the absence of the service is of no consequence in the sense that there is no loss that would have been avoided but for the breach. Nevertheless, the party in breach should have to refund any payments made. We might characterise this as rescission and restitution upon a failure of consideration and that probably is an adequate description. But one might just as well say that return of the purchase price is compensation to the plaintiff for the protection expected and the proper measure of the failed expectancy. It would also be 'unjust' for the defendant to retain the contract price because the defendant did not provide the quid pro quo, and, in this sense, the case could take on some of the characteristics of restitution.

A breach of warranty provides another kind of compensation rule that may have results quite different from those in other contract cases. The standard measure is the difference in value between what was delivered and what was warranted. The contract price is not a cap, and the recovery may be substantially higher than the original contract price.[1] The compensation is not for a measurable loss but for a dashed hope. The law recognises in these cases something akin to a proprietary interest in the expectations aroused by the defendant's own touting. The recovery 'restores' the plaintiff's expectation and bears a resemblance to restitution, but is better characterised as a species of promissory enforcement.

Waddams eventually concludes that restitution for an unjust enrichment in a breach of contract case is appropriate only when three requirements are satisfied.[2] There are cases which fit these requirements, but the classification may be both too broad and too narrow.

First, the plaintiff in almost every breach of contract case may be said to have suffered the loss of an opportunity to bargain. That requirement does little to identify the appropriate cases for a restitutionary recovery.

Second, the plaintiff who has an interest that could be protected by the intervention of equity may present a stronger case for a restitutionary remedy for a sharing of the proceeds. Disgorgement of the profits might be a substitute for an equitable order. Consider, for example, the hypothetical case of a famous athlete who breaches a contract to take advantage of a high paying opportunity. With adequate notice the other party might be able to enjoin the athlete from undertaking the other opportunity although equity would be unlikely to force him to perform the original agreement.[3] Without sufficient notice, the other party's only remedy would be damages. Measuring the damage recovery by the gain from the breach might be useful as a post hoc substitute for injunctive relief.

Third, the plaintiff who has a proprietary interest in information that the defendant was contractually bound not to disclose might obtain similar relief.

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1 See eg *Chatlos Sys Inc v National Cash Register Corp* 670 F 2d 1304 (3d Cir), cert dismissed, 457 US 1112 (1982); *Smith v Pembridge Associates Inc* 440 Pa Super 410, 655 A 2d 1015 (1995).

2 (1997) 11 *JCL* 115.

3 The leading cases continue to be *Lumley v Gye* (1853) 2 E & B 216; 118 ER 749 and *Lumley v Wagner* (1852) 1 De GM & G 604; 42 ER 687. See generally Howard O Hunter, *Modern Law of Contracts*, Warren Gorham & Lamont Inc, Boston, §13.05 (rev ed 1993 and supp 1996-2).

In the United States the *Snepp* case is the analogue to the *Spycatcher* case. Frank Snepp, a former CIA agent, wrote a 'kiss and tell' book about his days in the spy business in violation of his contract with the CIA. The United States Supreme Court approved the imposition of a constructive trust in favour of the government on the royalties from the book.[4] Snepp's contract breach was also a form of 'taking' and the court reasoned that the government, which had a proprietary interest in the information, could recover the pecuniary value of the information taken.

There are some cases that do not fit the mold. The losing construction contract cases are among those. Neither a building contractor nor the owner can specifically enforce a construction contract. In a proper case, one party or the other might be able to get some form of injunctive relief, but the intervention of equity in such circumstances will be rare. The contractor has no more than the ordinary proprietary interest that is common to many different contracting parties. Nevertheless, upon a breach by the owner, the contractor can recover 'off' the contract for the fair market value of the goods and service provided to the date of breach even if that amount is substantially greater than the proportional recovery under the contract would be.[5] In the United States the majority rule is that the contract price is not a cap, and the contractor could wind up recovering more than the total contract price for work that is less than what was contemplated under the contract.[6] These cases do not involve restitution of profits derived from a breach, but they do result in the denial of any savings expected by the breaching party and the allocation of all risks of loss (those of both parties) to the breaching party.

In sum, Waddams has provided some rough guides for those relatively few cases in which restitution rather than traditional compensation seems to be the norm. His approach is helpful in analysing these situations and provides a basis for distinguishing the cases. On the whole, it may be just as well to treat these cases as anomalies — though not without justification — in the general scheme of compensatory damages.

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4 *US v Snepp* 444 US 507 (1980).

5 American Law Institute, Restatement (Second) of Contracts, §373(1) (1981). See eg *US v Algernon Blair Inc* 479 F 2d 638 (4th Cir 1973); *Scaduto v Orlando* 381 F 2d 587 (2d Cir 1967); *City of Philadelphia v Tripple* 230 Pa 480, 79 A 703 (1911).

6 See eg *IT Corp v Motco Site Trust Fund* 903 F Supp 1106 (SD Tex 1994). But cf *Johnson v Bovee* 40 Colo App 317, 574 P 2d 513 (1978).