

# Disgorgement for Breach of Contract: My Loss, Your Gain?

Jessica Rickett\*

## I. INTRODUCTION

Generally, the remedy available to an injured party following a breach of contract is monetary compensation, measured by that party's loss, not by the gain made by the party in breach.<sup>1</sup> This compensation is determined according to either of two interests: the expectation interest or the reliance interest.<sup>2</sup>

The purpose of the expectation measure is to place the injured party in the position it would have been in had the contract been performed, or as close as possible to that position as a monetary award could place them.<sup>3</sup> This measure has been the pre-eminent principle for awarding damages since the sixteenth century.<sup>4</sup> It was not until Fuller's and Perdue's famous 1930s essay<sup>5</sup> that significant notice was taken of the reliance measure.<sup>6</sup> The objective of this measure is to put the injured party in the position it would have been in had the contract never been made, by compensating it for expenses incurred in reliance on the contract.<sup>7</sup> The reliance interest is usually applied when it is not possible to ascertain the expectation interest of the injured party with sufficient certainty.<sup>8</sup>

These two interests generally provide an adequate compensatory remedial scheme to cover most cases of contractual breach. However, they do not afford a sufficient remedy in situations where the aggrieved

---

\* I would like to thank Charles Rickett and Ross Grantham for their continual encouragement, insight and patience.

<sup>1</sup> *Attorney-General v Blake* [1998] Ch 439, 456 (CA) per Lord Woolf MR

<sup>2</sup> *Surrey County Council v Bredero Homes Ltd* [1993] 1 WLR 1361, 1369 (CA) per Steyn LJ.

<sup>3</sup> *Robinson v Harman* (1848) 1 Ex 850, 855; see also Treitel, *The Law of Contract* (10 ed, 1999) 873

<sup>4</sup> Farnsworth, "Your Loss or My Gain? The Dilemma of the Disgorgement Principle in Breach of Contract" (1985) 94 Yale LJ 1339, 1351.

<sup>5</sup> Fuller and Perdue, "The Reliance Interest in Contract Damages" (1936-1937) 46 Yale LJ 52, 373.

<sup>6</sup> Farnsworth, *supra* note 4.

<sup>7</sup> *Anglia Television Ltd v Reed* [1972] 1 QB 60; see also Treitel, *supra* note 3, 875

<sup>8</sup> Virgo, *The Principles of the Law of Restitution* (1999) 498.

party has suffered no loss or has suffered only de minimis loss - and, therefore, has no thwarted expectation or reliance interest – yet the party in breach has made a resulting gain.

In cases such as these, the injured party seeking relief for a breach cannot receive compensation properly speaking because it is unable to establish loss. What is at issue, therefore, is whether the injured party can claim the profits made by the party in breach as an alternative remedy. In other words, can the injured party strip the breaching party of the gains made as a result of the breach? These gains can be loosely said to be “unjust gains” in the sense that they are the result of a wrong committed by the party in breach.

The object of this article is to determine whether any remedy exists for such cases and if so, what, if any, are the appropriate limitations to this remedy.

## II. A PROBLEM OF TERMINOLOGY: RESTITUTION FOR WRONGS OR DISGORGEEMENT?

In phrasing the desired remedy as being one “to strip the breaching party of its unjust gains”, it may be assumed that the cause of action in question must be located in unjust (or restorable) enrichment and, therefore, that the principles of the law of restitution apply. It is, however, essential to understand that, while the remedy sought is restitutionary in nature, the remedy is sought as a *response* to the civil wrong of breach of contract. It is this civil wrong that is the cause of action.<sup>9</sup> Hence, it is part of the law commonly referred to as “restitution for wrongs”.<sup>10</sup>

It is more appropriate, perhaps, to describe this gain-based remedy as something other than ‘restitution’, as restitution usually implies ‘giving back’ or ‘restoration’. What is at issue here, however, is the ‘giving up’ of a gain. The term ‘disgorgement’, meaning to compel the party in breach to give up what has been wrongfully obtained, more accurately reflects the object of this gain-based remedy<sup>11</sup> and will be used in place of ‘restitution’ throughout this article.

---

<sup>9</sup> Birks, *An Introduction to the Law of Restitution* (1985) 313.

<sup>10</sup> See, generally, English Law Commission, *Aggravated, Exemplary and Restitutionary Damages* (1997) paras 3.1-3.84.

<sup>11</sup> *Attorney-General v Blake* [2000] 3 WLR 625, 638 (HL) per Lord Nicholls, 644-645 per Lord Steyn; see also Grantham and Rickett, *Enrichment & Restitution in New Zealand* (1999) 472-473.

### III. DISGORGEMENT FOR BREACH OF CONTRACT?

While the availability of disgorgement for breach of contract has long been debated in academic writings, there has been a “surprising dearth of judicial decision”<sup>12</sup> on the subject. However, inconsistent and unclear reasoning has hampered the effectiveness of the decisions that have discussed or applied a disgorgement remedy. This may be because it is a “notoriously difficult subject”.<sup>13</sup> The courts have been quick to dismiss its potential role in favour of a strict application of compensatory principles,<sup>14</sup> or the simplistic imposition of a remedial constructive trust on the gains made by the party in breach.<sup>15</sup> To strictly apply compensatory principles, thereby denying any gain-focussed remedy, is a limited response by the courts to the consequences of a breach of contract. On the other hand, manipulating principles of equity to impose a remedial constructive trust over the breaching party’s profit is unnecessary where a comprehensive set of disgorgement rules can be formulated instead.<sup>16</sup>

Academic debate on the subject has also failed to offer a clear and foolproof solution to the problem:<sup>17</sup>

On the one hand, there is no or virtually no support for a general action for disgorgement of profits made by a contract breaker by reason of his breach. On the other hand, there is significantly absent from ... academic comment a reasoned statement of the particular circumstances when such a remedy should be available.

Such a statement would allow a disgorgement remedy in appropriate cases, without rendering the law uncertain and vulnerable to the subjective discretion of the court.

This article proposes a blueprint that will do just this without usurping the primary role of compensation for breach of contract. It will examine the most recent and influential decisions of the courts on the subject and

<sup>12</sup> Ibid 631 per Lord Nicholls

<sup>13</sup> Ibid 645 per Lord Steyn

<sup>14</sup> *Tito v Waddell (No 2)* [1977] Ch 106, 332

<sup>15</sup> *Snepp v United States* 444 US 507 (1980), see also *News Ltd v Australian Rugby Football League Ltd* (1996) 139 ALR 193, 291

<sup>16</sup> Compare the failed attempt to do this in *Fortex Group Ltd (In Receivership and Liquidation) v MacIntosh* [1998] 3 NZLR 171 (CA). Discretionary proprietary remedies in equity raise difficult problems which would be likely to be avoided if a more effective disgorgement regime existed. See Grantham and Rickett, *supra* note 11, 403-419, Birks, “Rights, Wrongs and Remedies” (2000) 20 OJLS 1

<sup>17</sup> *Supra* note 11, 644 per Lord Steyn

the issues that they raise. It will also discuss any issues that have arisen from academic writings that require consideration and assessment. Finally, it will conclude with the proposed blueprint itself.

#### IV. *WROTHAM PARK ESTATE CO LTD V PARKSIDE HOMES LTD*

In *Wrotham Park Estate Co Ltd v Parkside Homes Ltd* (“*Wrotham Park*”),<sup>18</sup> the defendant developer acquired land subject to a restrictive covenant in favour of the adjoining estates owned by the plaintiff. In breach of this restrictive covenant, the defendant commenced building on a housing development without first obtaining consent from the plaintiff. The plaintiff had specified that it would not, under any circumstances, consent to any sort of relaxation of the covenant and sought restraining and mandatory injunctions to prevent further building and to demolish what had been built.

Brightman J refused to grant an injunction on the grounds that it would be an “unpardonable waste of much needed houses”.<sup>19</sup> His Honour did, however, award damages to the plaintiff. Brightman J held that the breach of the restrictive covenant was an interference with the plaintiff’s proprietary right in the covenant and therefore that it was entitled to damages under Lord Cairns’ Act.<sup>20</sup>

Notwithstanding that the value of the adjoining estate had not diminished and, therefore, that the plaintiffs had not suffered loss from the breach of the covenant, Brightman J awarded what he regarded as compensatory damages; assessed as the sum that might reasonably have been demanded for the relaxation of the covenant, namely five per cent of the profits anticipated to be earned from the sale of the houses.

While the finding that damages are available where a proprietary right has been interfered with is consistent with previous cases,<sup>21</sup> Brightman J’s classification of the measure of damages as compensatory has been demonstrated to be flawed.<sup>22</sup> It was clear that the plaintiffs would never

---

<sup>18</sup> [1974] 1 WLR 798 (Ch D)

<sup>19</sup> *Ibid* 811

<sup>20</sup> Officially the Chancery Amendment Act 1858 (UK), s 2, and whilst it has now been repealed, jurisdiction still remains empowering the Court of Chancery to award damages in substitution for an injunction or specific performance, see, in New Zealand, the Judicature Act 1908, s 16A

<sup>21</sup> See *Watson, Laidlaw & Co Ltd v Pott, Cassels, and Williamson* (1914) 31 RPC 104, 119 per Lord Shaw, *Strand Electric and Engineering Co Ltd v Brusford Entertainments Ltd* [1952] 2 QB 246

<sup>22</sup> O’Dair, “Resitutionary Damages for Breach of Contract and the Theory of Efficient Breach Some Reflections” (1993) 46 CLP 113, 126

have consented to the relaxation of the covenant and, therefore, no expectation loss arose. Rather, as Steyn LJ recognised in *Surrey County Council v Bredero Homes Ltd* (“*Bredero Homes*”),<sup>23</sup> “[t]he object of the award ... was not to compensate the plaintiffs for financial injury, but to deprive the defendants of an unjustly acquired gain”,<sup>24</sup> and was, therefore, a disgorgement remedy.

Brightman J’s decision was recently approved by a majority of the House of Lords in *Attorney-General v Blake*,<sup>25</sup> who upheld *Wrotham Park* as good law “showing that in contract ... damages are not always narrowly confined to recoupment of financial loss. In a suitable case damages for breach of contract may be measured by the benefit gained by the wrongdoer from the breach”.<sup>26</sup>

## V. *SURREY COUNTY COUNCIL V BREDERO HOMES LTD*

The rule established in *Wrotham Park* was tested in *Bredero Homes*. The plaintiffs were local authorities who each held the fee simple in adjoining pieces of land. The land was sold to the defendant developer subject to a covenant that provided that the land could only be developed in accordance with planning permission approved by the plaintiffs. This permission was for 72 houses, a limit imposed solely so that the defendant would have to pay additional monies to the plaintiffs if it built additional houses.

In breach of the covenant, the defendant obtained a new planning permission to build 77 houses,<sup>27</sup> thereby making an increased profit from the 5 additional houses.

It was clear that the defendant had breached the contract, but it was equally clear that the plaintiffs had suffered no loss. The plaintiffs nevertheless claimed damages, quantified either as the profits made by the defendant as a consequence of its breaching the covenant, or as that part of the profit that represented a reasonable price for the relaxation of the covenant (in accordance with the *Wrotham Park* approach).

---

<sup>23</sup> Supra note 2

<sup>24</sup> Ibid 1369

<sup>25</sup> Supra note 11

<sup>26</sup> Ibid 637 per Lord Nicholls

<sup>27</sup> Oddly, permission was granted by one of the plaintiff councils for the new plans on the basis that it could not be refused because the council was bound by a statutory duty to allow it

The Court of Appeal considered both methods of quantification to be restitutionary<sup>28</sup> and, therefore, discussed the availability of disgorgement (restitutionary) damages for breach of contract. The Court unanimously dismissed the plaintiff's claim for disgorgement, but each judge's reasons for doing so differed.

Of the three judgments, Steyn LJ's was, with respect, the only one of real substance and, accordingly, has attracted discussion in later cases and academic writing.<sup>29</sup> However, it is necessary for the sake of completeness to mention the two other judgments before examining Steyn LJ's in some detail.

Rose LJ preferred to distinguish *Wrotham Park* on the grounds that there the plaintiff had objected to the building as soon as it learned of it and had sought restraining and mandatory injunctions. It had taken exception to the building throughout and his Lordship considered the result to be "unsurprising" and necessary to "achieve a just result".<sup>30</sup> The plaintiff was entitled to some sort of remedy. Conversely, in *Bredero Homes*, the plaintiffs did not object to the additional houses and had in fact indicated a willingness to vary the covenant.<sup>31</sup>

This distinction is unconvincing for two reasons. First, the availability of relief in contract should not depend upon whether the injured party sufficiently objected to the breach, but on the actual rights acquired as a result of the contract, which the law ought to uphold. The parties had freely consented to the covenant and the defendant had breached it. Relief is dependent upon the establishment of a contractual wrong, not on how significantly the injured party objects to that wrong.

Second, on its own terms, *Wrotham Park* was not decided on the ground that the plaintiff would never have consented to a relaxation of the covenant,<sup>32</sup> but on the basis that the restrictive covenant vested a proprietary right in the plaintiff which had been interfered with. It was this interference that entitled the plaintiff to relief.

Dillon LJ sought to distinguish *Wrotham Park* on the basis that the remedy sought in that case was equitable, whereas damages at common law are compensatory. In doing so, his Lordship nevertheless recognised the principle laid down by Lord Wilberforce in *Johnson v Agnew*<sup>33</sup> that

---

<sup>28</sup> Supra note 2

<sup>29</sup> Burrows, "Case and Comment No Restitutionary Damages for Breach of Contract *Surrey C C v Bredero Homes*" [1993] LMCLQ 453, 458

<sup>30</sup> Supra note 2, 1371 per Rose LJ

<sup>31</sup> Ibid

<sup>32</sup> This fact was, in actuality, cast aside by the award of "compensatory" damages, see text supra Part IV

<sup>33</sup> [1980] AC 367

there is no warrant for the court to award equitable damages under the Lord Cairns' Act any differently from common law damages. However, because *Johnson v Agnew* had not been cited to Brightman J in *Wrotham Park* the case was decided solely by reference to equitable rules.<sup>34</sup> Dillon LJ held that in the instant case the remedy could not be equitable because the plaintiffs had not applied for specific performance or an injunction and that, accordingly, only the common law rules relating to damages could apply. Hence, in accordance with the principle that damages are compensatory, his Lordship ruled that damages for breach of contract "do not cover an award, to a plaintiff who has himself suffered no loss, of the profit which the defendant has gained for himself by his breach of contract".<sup>35</sup>

Dillon LJ's reasoning, while perhaps logically supportable, is not particularly satisfactory in light of the well-established principle in *Johnson v Agnew* that his Lordship himself mentioned. While approving the doctrine that equitable damages, awarded under the jurisdiction of Lord Cairns' Act, and common law damages should be assessed on the same principles, his Lordship then declared that gain-based remedies (which are readily available in equity and in respect of some torts and, it would seem, in the peculiar statutory jurisdiction) are not available for breach of contract. As Burrows<sup>36</sup> articulately states, Dillon LJ "was guilty of riding two different horses at the same time".<sup>37</sup> In doing so, the result is an attractive but fatally flawed decision that adds no weight to the issue of the availability or non-availability of disgorgement damages for breach of contract.

Steyn LJ's judgment has received the most attention from academics and has usually been the judgment referred to by the courts when discussing *Bredero Homes*.<sup>38</sup> His Lordship noted that while disgorgement is not traditionally available for breach of contract, "a coherent law of obligations must inevitably extend its protection to cover certain restitutionary interests".<sup>39</sup> Steyn LJ believed the issue to be, not whether disgorgement is available at all, but the extent of the limitations to its availability.

Steyn LJ, in approving *Wrotham Park*, clearly regarded the award as an example of disgorgement damages, regardless of Brightman J's

---

<sup>34</sup> Supra note 2, 1366-1367

<sup>35</sup> Ibid 1365

<sup>36</sup> Professor of Law at the University of Oxford

<sup>37</sup> Burrows, supra note 29

<sup>38</sup> See, for example, supra note 1, 457 per Lord Woolf MR, *Jaggard v Sawyer* [1995] 1 WLR 269, 291 per Millett LJ

<sup>39</sup> Supra note 2

comments when making the award that it was compensatory. This is reinforced by academic comment that the damages in *Wrotham Park* were never truly compensatory but were merely disguised as such.<sup>40</sup> However, his Lordship limited the availability of disgorgement damages for breach of contract to cases of invasion of property rights created or secured under the contract, adding that “property ... must be interpreted in a wide sense”.<sup>41</sup> In applying this “test” to the facts of *Bredero Homes*, his Lordship decided, after careful consideration of several policy factors, that extending the law of disgorgement damages to include breach of contract generally would be unsound policy. His Lordship held that even after interpreting property in its broadest sense, the covenant was not a property right.<sup>42</sup> Therefore, there could be no invasion of property rights as required for an award of disgorgement damages.<sup>43</sup>

Steyn LJ did not provide any substantial reasoning when classifying contractual rights as non-proprietary. Instead, his Lordship seemed to accord much weight to several policy factors, primarily concerning economic efficiency. Steyn LJ put forward five main reasons why disgorgement damages should not normally be awarded for a breach of contract:<sup>44</sup>

1. It should not be available simply because discretionary equitable remedies are available;
2. Such a remedy would focus on the motive of the party in breach. This is contrary to the approach of the law of contract to breach and would “lead to greater uncertainty in the assessment of damages in commercial ... disputes”;<sup>45</sup>
3. Such a remedy would confer a windfall on the plaintiff;
4. Such a remedy would have a tendency to discourage economic activity; and
5. Such a remedy would result in higher insurance premiums because the level of insured liability risks would increase.

While Steyn LJ’s view that it is desirable to extend the availability of the remedy of disgorgement is correct, his Lordship failed to reach that

---

<sup>40</sup> See, for example, O’Dair, *supra* note 22, Goodhart, “Restitutionary Damages for Breach of Contract The Remedy that Dare Not Speak its Name” (1995) 3 RLR 3, 7-8

<sup>41</sup> *Supra* note 2, 1370

<sup>42</sup> The covenant in this case was a mere contractual right, in contrast to the *restrictive* covenant in *Wrotham Park* that was a proprietary right

<sup>43</sup> *Supra* note 2, 1371

<sup>44</sup> *Ibid* 1370

<sup>45</sup> *Ibid*

conclusion using sound reasoning or coherent legal principle. His Lordship's classification of contractual rights as generally non-proprietary is discussed below in Part V.1. It can be supported, it will be demonstrated, by analysing the nature of proprietary and personal rights. His Lordship's arguments of economic efficiency are discussed in Part V.2.

## 1. Proprietary Rights and Specific Performance

There has been much debate over the extent of the reach of the notion of 'property', particularly in relation to the classification of contractual rights. The essence of the conflict lies in determining the significance that the law accords to contractual promises. Perhaps the most notable contribution to this conflict was made by Oliver Wendell Holmes:<sup>46</sup>

It is true that in some instances equity does what is called compelling specific performance .... This remedy is an exceptional one. The only universal consequence of a legally binding promise is, that the law makes the promisor pay damages if the promised event does not come to pass. In every case it leaves him free from interference until the time for fulfilment has gone by, and therefore free to break his contract if he chooses.

Holmes advocated that the principal right of parties to a contract is to damages in the event of breach, not to specific performance of the contractual promise. A contract is the taking of a risk, creating a liability to pay damages if the promised event does not occur. "If you commit a contract you are liable to pay damages, unless something happens, *i.e.*, performance, over which you may or may not have control".<sup>47</sup> Thus, proponents of this view deny that a contractual right has a proprietary character upon which a contracting party can rely to demand performance, consistent with Steyn LJ's analysis in *Bredero Homes*.

However, while the conclusion that contractual rights are not proprietary in nature is correct, Holmes' reasoning, it is suggested, is flawed. His argument concentrates on the remedy available and assumes that it is always a perfect substitute for the right of performance.<sup>48</sup> This would mean that a party to a contract is freely allowed to breach the contract and that the reasonable expectations of the other party are disappointed. This is misconceived. A party does not enter a contract in

---

<sup>46</sup> Howe (ed), *The Common Law By Oliver Wendell Holmes* (1967) 236

<sup>47</sup> Buckland, "The Nature of Contractual Obligation" (1944) 8 Cambridge L J 247

<sup>48</sup> Friedmann, "The Efficient Breach Fallacy" (1989) 18 J Legal Stud 1

order to purchase a right to a remedy but rather a right to performance which, upon failure, is vindicated by the remedy. “One does not buy a right to damages, one buys a horse.”<sup>49</sup> The failure to deliver the horse is the breach that is to be remedied.

While it is accepted that a person cannot be compelled to perform their contractual promises, it is not a necessary consequence of this that the payment of damages is the proper obligation.<sup>50</sup> This would mean that it would not be wrong to breach a contract, and for specific performance not to be granted.<sup>51</sup> The commercial implications of this are staggering. Parties would be unable to rely on the contractual promises made to them and would not be entitled to hold the reasonable commercial expectations which the contract was originally formed to create, encourage, and protect. If parties are denied the right to rely on promises made, they would cease to contract unless they could be certain that any available remedy was equal to or greater than the value of the performance for which they contracted. Even if damages did equate to such an amount (the expectation interest rather than the reliance interest), parties would still have to consider transactional costs incurred that are not generally included in the calculation of damages as of right. Such expenses would include the costs of litigation and of seeking and securing alternative sources of performance. An incalculable, and perhaps more significant, cost is the damage to the relationship between the contracting parties, as the injured party may no longer place reliance on promises made by the party in breach.

Some argue that contractual rights are not proprietary, primarily on the grounds that they are not *per se* enforceable, except in the sense that a breach of these rights triggers a right to a remedy of damages. This argument dismisses the very purpose for which the institution of contract exists, namely, the protection and enforcement of reasonable bargains made voluntarily between parties.

A contract is a source of rights, both personal and proprietary. The making of a contract is an event which brings such rights into being. Thus, the classification of contractual rights cannot be determined by reference only to the institution of contract itself, but must be determined in light of the distinction between property rights and personal rights.

---

<sup>49</sup> Quoted in Buckland, *supra* note 47

<sup>50</sup> Jones, “The Recovery of Benefits Gained from a Breach of Contract” (1983) 99 LQR 443, 453-454

<sup>51</sup> *Ibid*

“The distinction lies in the identity of the subject of the obligation that the right reflects.”<sup>52</sup> Personal rights (rights in personam) are rights enforceable against a particular person or group of persons, whereas property rights (rights in rem) attach to a particular object and are enforceable against the world. Thus, the obligation is not owed to an individual right-holder, but to the whole world in respect of the object. A right in rem remains enforceable even when it is transferred or assigned to another, while a right in personam only exists as between the right-holder and the person that owes the duty to the right-holder.

It thus remains to examine the nature of contractual rights in light of this distinction. It would be absurd to assume that simply because A can enforce its contractual rights against the other contracting party, B, that those rights are necessarily ipso facto proprietary rights. It is the nature of the obligation that those promises create, whether they are proprietary or merely personal, that is the key issue. In *Wrotham Park* the contractual right in question was a restrictive covenant which created a right in rem. The right, created contractually, was greater than a personal right as against the other contracting party. As a right in rem, it could be transferred to any person and required every person to comply with the restrictive covenant when dealing with the land to which it was attached. However, in *Bredero Homes* the restrictions relating to the piece of land were not covenanted but were merely agreed upon as terms of the parties’ contract. Thus, the rights of the local authorities to allow or deny extra housing was a right in personam that only the developers were obliged to respect. If rights in personam were accorded the same weight as rights in rem, the result would be that once a party has contracted to hold a certain right, it would be entitled to demand that every person was under a duty or obligation to respect that right. In other words, by gaining the consent of one party to be bound to a particular obligation, it would effectively bind the whole world to uphold the right that it contracted for. This is inconsistent with the very nature of a contract, which is essentially a vehicle essentially for the assumption of (personal) obligations between parties. It is only a mechanism for the creation of property rights in limited and express cases.<sup>53</sup>

Therefore, a contractual right can never be given the standing of a proprietary right merely because it is contractual. There must be evident

---

<sup>52</sup> Grantham and Rickett, *supra* note 11, 31, see also Smith, “Disgorgement of the Profits of Breach of Contract Property, Contract and ‘Efficient Breach’” (1994-95) 24 Can BLJ 121, 132, Rickett and Grantham, “The Propylaeum of Property Rights” [2000] NZLJ 103

<sup>53</sup> It is often overlooked that conveyance of property rights is a distinctive analytical step, even in cases of sale and purchase

in its creation an obligation that is universally owed to all the world in respect of the subject of the right created. Accordingly, although Steyn LJ's reasoning may have been somewhat truncated, his Lordship's refusal to declare contractual rights to be proprietary was clearly correct.

One of Steyn LJ's objections to extending the availability of disgorgement was that such a remedy is not related to discretionary equitable remedies. In dismissing the argument that disgorgement should be limited to those cases where remedies of specific performance and injunction can be granted, as "a bromide formula",<sup>54</sup> his Lordship seems, with respect, to contradict himself. The phrase "bromide formula" can be interpreted in two ways. It can be taken to suggest that a test based on the availability of such remedies would be too exact and specific, leaving no room for adjustment where it is found to be unsatisfactory. Alternatively, it can mean that such an argument is a "soothing platitude or trite remark"<sup>55</sup> that proffers an easy solution that is not well thought out or contemplated. On either interpretation, the effect of the argument is that if such a definitive and restrictive test were adopted it may not be sufficiently comprehensive.

Yet his Lordship, perhaps unwittingly, adopts an alternative test that is just as much "a bromide formula". Limiting disgorgement to cases where a proprietary right has been interfered with seems also to be definite and restrictive. Thus, while rejecting one possible test because it is not sufficiently comprehensive, another is adopted that is equally insufficiently comprehensive. The substantive reasoning for adopting one and not the other lies not in its effect on application, but in respect of the rights which it seeks to enforce. Restricting the availability of disgorgement to cases where equitable relief could be ordered is incorrect because the absence of a right to "equitable" relief in the form of specific performance or injunction does not always indicate an "absence of merit".<sup>56</sup> It does not follow that because "equitable" relief is not appropriate in some cases, that disgorgement must also be refused in these cases as a consequence. Equitable relief is justified where the defendant has acted unconscionably as determined by the application of specific equitable principles. The courts have, however, consistently denied that the availability of disgorgement should be based on the quality of the breach by the defendant. Whether the breach is cynical or deliberate is

---

<sup>54</sup> *Supra* note 2, 1370.

<sup>55</sup> Brown (ed), *The New Shorter Oxford English Dictionary* (4 ed, 1993) Vol I 287.

<sup>56</sup> Goodhart, *supra* note 40, 11.

irrelevant in determining the correct remedy.<sup>57</sup> First, there is great practical difficulty in determining what is cynical or deliberate activity<sup>58</sup> and, second, the law of contract is not usually concerned with the breaching party's motives but rather with upholding the bargain struck between the contracting parties.

The equitable remedies available for the cause of action of breach of contract are irrelevant to the availability of disgorgement, not because they result in "a bromide formula", but because they are founded on a concept foreign to the law of contract. They seek, in essence, to prevent unconscionable actions, while contract law seeks only to enforce the bargains of the parties or to compensate for failures in such bargains.

To determine whether the injured party is entitled to the breaching party's profits, it is necessary to determine the sort of rights with which the party in breach has interfered. The law will always respond to an invasion of proprietary rights:<sup>59</sup>

If the plaintiff can be said to have a proprietary interest in the subject matter of the contract, there is a case for requiring the contract breaker to account for profits, for it can be said that the wrongdoer has derived a profit from something that belonged to the plaintiff.

Hence, if the injured party can establish that its contractual rights were proprietary, it must be allowed the profits gained directly from any interference with those rights, even where the interference is by means of a breach of contract. However, it is essential to recognise that the proprietary interest approach is an appropriate test, not because it is considered not to be a bromide formula, but because its theoretical foundation on the analysis of rights is correct.

Something more is required to define the availability of the remedy of disgorgement. If the remedy remains limited to interferences with property rights, there will still remain cases where the injured party will not be eligible for a remedy simply because either it suffered no direct loss, or its particular contractual rights fell short of amounting to proprietary rights. Lord Nicholls noted this concern in *Attorney-General v Blake* (HL). While recognising that property rights are superior to mere contractual rights, his Lordship queried whether such a test could be

---

<sup>57</sup> Supra note 2, 1370 per Steyn LJ, supra note 1, 457 per Lord Woolf MR, supra note 11, 640 per Lord Nicholls. This argument was one of the five objections raised by Steyn LJ in *Bredero Homes* to extending the availability of disgorgement.

<sup>58</sup> There must be a serious risk of adopting an ex post facto approach informed by hindsight.

<sup>59</sup> Waddams, "Profits Derived from Breach of Contract: Damages or Restitution" (1997) 11 JCL 115, 121.

wholly correct where the result is that, “as between the parties to a contract, a violation of a party’s contractual rights should attract a lesser degree of remedy than a violation of his property rights”.<sup>60</sup> This would be a “sorry reflection on the law”.<sup>61</sup> Furthermore, Professor Friedmann<sup>62</sup> writes that “[i]n modern commercial-industrial society, contractual rights constitute a major form of wealth, and consequently their adequate protection becomes of the utmost importance”.<sup>63</sup>

Therefore, it remains necessary to extend the availability of disgorgement beyond interferences with proprietary rights to a position that provides an adequate gain-focussed remedy to the injured party.

## 2. Economic Efficiency

Steyn LJ relied heavily on arguments of economic efficiency to deny the extension of a disgorgement remedy for breach of contract. The arguments are based loosely on a widely held view that the law should facilitate the maximisation of wealth and efficiency.<sup>64</sup> If a party to a contract has the opportunity to pursue a more profitable activity, but must breach a contract in order to do so, the objective of economic efficiency deems such an “efficient breach” to be permissible. The only obligation on the party in breach is to pay the injured party expectation damages. To deny the party in breach this right would result in a disadvantage to society because the greatest possible profit would not have been made, thereby failing to maximise wealth creation.

The argument continues that, in relation to the two contracting parties, such a breach benefits both parties. The injured party is placed in the position it expected to be in had the contract been performed, by the receipt of damages compensating that party’s expectation interest, and the party in breach is in a better position than it would have been had the contract been performed.<sup>65</sup> However, this can only be so where the injured party can calculate its expectation interest with sufficient certainty. As discussed,<sup>66</sup> cases arise where the injured party cannot make such a calculation and cannot, therefore, quantify its loss. The injured party in this situation will not be better off because its expectations of

---

<sup>60</sup> Supra note 11, 637

<sup>61</sup> Ibid

<sup>62</sup> Professor of Law at Tel Aviv University

<sup>63</sup> Friedmann, supra note 48, 23-24

<sup>64</sup> See, generally, Posner, *Economic Analysis of Law* (5 ed, 1998)

<sup>65</sup> Friedmann, supra note 48, 3

<sup>66</sup> See text supra Part I

performance have not been fulfilled and it is unable to receive compensation. The breach has not, therefore, been wholly efficient, but merely profitable to the party in breach.

In addition to this deficiency in respect of its coverage, there are fundamental errors in the application of the rule of maximisation of wealth to breach of contract. Advocates of the economic efficiency argument misuse the principle upon which it is based. This principle, known as the Coase Theorem, states that, apart from transaction costs, wealth or efficiency must be measured by its total effect not simply its distributional effect: in other words, its effect on society as a whole.<sup>67</sup> An action is wealth-maximising if it benefits society as a whole; it is irrelevant to whom the benefit actually accrues. Thus, where A breaches its contract with B, making a direct profit of \$100 which A is then required to pay to B as disgorgement, the breach has maximised the wealth of society by \$100, regardless of who actually receives the profit.<sup>68</sup> Awarding the remedy of disgorgement, therefore, does not prevent economic efficiency: it merely affects how the fruits of the efficient breach are distributed.

In this respect, the effect of disgorgement is the same as that of compensation. Consider the same situation but with an award of compensation of \$50 instead. A keeps \$50 and B receives the calculable expectation interest of \$50. The net profit to society of \$100 remains the same. The distribution of the profit “is an immaterial detail according to economic analysis; the point is that social wealth has increased”.<sup>69</sup>

An objection to this analysis is that if A knows that it will be liable in disgorgement, critics argue that A will choose not to breach the contract and the opportunity to profit will be lost. Thus, it is said that disgorgement deters wealth-maximising behaviour to the detriment of social wealth. As Smith<sup>70</sup> argues, this objection is again theoretically flawed because the critics fail to take account of all the economic factors which culminate in the principle of economic efficiency.<sup>71</sup> One key factor is the assumption that individuals are rational, value-maximising human beings. Under such an assumption, where a more profitable opportunity arises for one party, that party will enter into negotiations with the other contracting party to reach some sort of compromise. Using the same example, A will not offer more than \$100 because that is the extent to

---

<sup>67</sup> Coase, “The Problem of Social Cost” (1960) 3 J L & Eco 1, 44.

<sup>68</sup> Smith, *supra* note 52, 133.

<sup>69</sup> *Ibid* 134.

<sup>70</sup> Associate Professor of Law at McGill University.

<sup>71</sup> Smith, *supra* note 52, 133.

which A will profit from the breach, and B will not accept less than \$50 for that is what B will stand to lose if the contract is not performed. Thus, the party in breach will first compromise on the allocation of profits so that it can personally profit, to some extent at least, from the wealth gained from the breach.

Consequently, critics of disgorgement argue that the process of compromising incurs additional negotiating costs that are economically inefficient. The fact that such a compromise will incur negotiating costs, which are an exception to the reach of the Coase Theorem, is not a sufficient reason to deny disgorgement on the grounds of economic efficiency. If remedies were restricted to compensation only, both parties would incur litigation costs that could well exceed the negotiation costs of the contracting parties, as rational, value-maximising human beings. Hence, while negotiating costs may be incurred, which reduce the efficiency of the breach, the alternative to disgorgement is compensation only. This incurs transactional costs of litigation, which are equally as inefficient.

It is clear that disgorgement neither prevents nor discourages economic efficiency, because the theory of economic efficiency relies on the notion of rational, value-maximising individuals who will negotiate a release from a contract to gain a profit from an alternative opportunity. Disgorgement is concerned with the allocation of wealth already earned, not with the prevention of such wealth creation. On a proper construction of the theory of economic efficiency, it is extremely difficult to argue that disgorgement prevents economic efficiency.

However, the Court of Appeal, in its subsequent decision in *Attorney-General v Blake*,<sup>72</sup> found Steyn LJ's arguments of economic efficiency to be "persuasive reasons why such circumstances [in which disgorgement is available] should remain exceptional".<sup>73</sup> But, interestingly, none of the members of the House of Lords, on appeal in *Attorney-General v Blake*,<sup>74</sup> acknowledged the relevance of such arguments, let alone gave them any substantial weight. Such an absence of attention from their Lordships on the argument of economic efficiency (in a case well-argued by both counsel) can perhaps be interpreted as an authoritative rejection of its relevance, and perhaps even its validity, in judicial analysis.

It is noted that one of the leading advocates of "efficient breach", Judge Posner, asserts that where a breach is opportunistic, disgorgement should be allowed in order to strip the party in breach of *all* the profits

---

<sup>72</sup> Supra note 1.

<sup>73</sup> Ibid 457.

<sup>74</sup> Supra note 11.

made directly from the breach.<sup>75</sup> Yet, this position seems to contradict his argument that a breach should be allowed if it is economically efficient in creating more wealth than would have been created had the contract not been breached. Surely, a party acts “opportunisticly” when breaching a contract to make an increased profit. This is precisely the objective that Judge Posner argues that the law should facilitate, under the guise of “economic efficiency”.

While the notion of opportunistic breach has not been discussed by the courts in any case involving disgorgement,<sup>76</sup> it does indicate the conceptual weaknesses of the theory of economic efficiency and the danger of its apparently simplistic, common sense approach. It is suggested that to rely so heavily on such a theory, as Steyn LJ appears to have done in *Bredero Homes*, is to fall into the trap of superficially attractive arguments which, on closer analysis, have little or no merit. Economic efficiency is simply not a ground upon which the availability or non-availability of a disgorgement remedy can justifiably be determined.

## VI. *ATTORNEY-GENERAL V BLAKE* IN THE COURT OF APPEAL

The facts of *Attorney-General v Blake*<sup>77</sup> are unique. The defendant was employed by the Crown as a member of the Secret Intelligence Service. As such, he was subject to provisions of the Official Secrets Act (UK) in addition to a contractual undertaking not to divulge any official information gained as a result of his employment. He breached these obligations by providing information to the Soviet Union and was convicted under the Official Secrets Act. He escaped from prison and fled to Moscow, where he wrote an autobiography that included official information obtained in his capacity as a Crown employee. The book was subsequently published in the United Kingdom without the Crown’s consent. The Crown sued the defendant for breach of fiduciary duty owed by him as an employee claiming, as a consequence, beneficial ownership of the copyright and related royalties.

---

<sup>75</sup> Posner, *supra* note 64, 130-131.

<sup>76</sup> This is simply because the motive of the party in breach has been considered irrelevant, see text *supra* Part V.1.

<sup>77</sup> *Supra* note 1.

At first instance, the action failed on the ground that the duty of confidence owed by the defendant could not extend to information that was no longer confidential. The Attorney-General appealed.<sup>78</sup>

On appeal the action for breach of fiduciary duty was again dismissed, on the basis that such a duty lasted only as long as the fiduciary relationship lasted and the information remained confidential. While the Court held that the defendant's actions amounted to a clear breach of his contractual undertaking not to disclose the information,<sup>79</sup> the Crown had neither sought an equitable remedy in respect of the breach, nor could it establish any loss to justify a compensatory award for breach of contract.

In the course of the hearing, the Court invited submissions as to whether, "in the particular circumstances of the present case, the Crown might have a private law claim to restitutionary damages for breach of contract".<sup>80</sup> The invitation was, not surprisingly, rejected by the Attorney-General, following the decision in *Bredero Homes*. Disgorgement had been tightly restricted to cases of interference of proprietary rights and, following Steyn LJ's decision, the appellant's contractual rights against the defendant were not sufficient to amount to proprietary rights in accordance with his Lordship's preferred interpretation. Nevertheless, the Court of Appeal suggested, obiter dicta, that disgorgement could be a valid remedy where a reasonably well-defined set of criteria are met.<sup>81</sup>

The Court, in a single judgment delivered by Lord Woolf MR, began by recognising that damages for breach of contract are generally compensatory but, noting both academic and judicial criticism, stated that it was not a rule without exception; the major exception being the precedent set by *Wrotham Park*.

The proposition that disgorgement should only be available where a proprietary right is interfered with was quickly dismissed by a simple declaration that "the measure of damages cannot depend on whether the proceedings are between the original parties to the contract or their successors in title".<sup>82</sup> As discussed, this reasoning is conceptually

---

<sup>78</sup> The Attorney-General made an additional claim in public law, namely, that he had a duty to ensure the enforcement of the criminal law. The Court of Appeal upheld the public law claim and granted an injunction restraining the defendant from receiving any further royalties from the publication of the book.

<sup>79</sup> *Supra* note 1, 455 per Lord Woolf MR.

<sup>80</sup> *Ibid* 456.

<sup>81</sup> Perhaps what was most extraordinary, and which was acknowledged by the Court itself, was that such an exposition on the availability of disgorgement was not necessary to the actual case at hand because the decision was based on the entirely separate public law claim. See Chen-Wishart, "Restitutionary Damages for Breach of Contract" (1998) 114 LQR 363, 363-364.

<sup>82</sup> *Supra* note 1, 457.

unsound because the essential distinction between proprietary rights and the obligations they create, and personal rights, was not considered. The measure of damages does not depend on who the parties to the contract are but on the type of obligations created by the contract.

This flaw in the judgment of the Court of Appeal is not of significant effect, however, because it is not a crucial or foundational point of the judgment. Rather, the Court sought to move away from the notion of proprietary rights and to base the availability of disgorgement on different grounds informed by other considerations.

Such considerations could not include the moral culpability of the party in breach,<sup>83</sup> nor whether the breach enabled them to enter into a more profitable contract, nor whether in entering into the more profitable contract the party in breach had put it out of its power to perform the original contract.<sup>84</sup> This would seem to exclude any argument of economic efficiency as a justification for breach, even though the Court noted that Steyn LJ's objections to disgorgement, based on economic efficiency, were persuasive.

According to the Court of Appeal, there are two necessary conditions that must be met before an injured party can claim a remedy in disgorgement. First, the profit must be derived directly from the breach and, second, compensation must be inadequate.<sup>85</sup>

## 1. Profit Derived Directly from Breach

The first condition, that the profit must be derived directly from the breach, does not raise any conceptual difficulties, and is necessary to ensure that the injured party receives only the profit that accrued to the party in breach as a result of the breach. However, it is important to note that practical difficulties may arise where the party in breach can argue that, although the opportunity to profit could only be taken by breaching the contract, such profit did not result solely because of the breach but required something more from that party, such as its special skill or knowledge. A situation such as this may require a result similar to that reached in *Boardman v Phipps*,<sup>86</sup> a case of breach of fiduciary obligations. In that case, one of the defendants breached his fiduciary obligations, subsequently making a profit. While the defendant fiduciary was made to account for his profit to the plaintiff beneficiary, the House of Lords made

---

<sup>83</sup> Ibid.

<sup>84</sup> Ibid 458.

<sup>85</sup> Ibid.

<sup>86</sup> [1967] 2 AC 46.

an allowance for the skill and expertise used by the defendant in making the profit.

## **2. Remedial Inadequacy and Legitimate Interests in Performance**

The second condition, that compensation be inadequate, has received substantial attention, particularly from critics of disgorgement. This article is based on the assumption that where compensation is inadequate, some other form of remedy is required to allay the injured party of an obvious wrong committed against it. Such an assumption preserves the primacy of compensation for breach of contract and turns to disgorgement only when absolutely necessary.

Chen-Wishart<sup>87</sup> argues, however, that if the remedial scheme of contract law is compensatory, as it is in the common law in general, any inadequacies in compensation as a remedy need to be addressed within the context of the law of compensation itself:<sup>88</sup>

The lack of “fit” is immediately apparent. If the concern really is about defects in the current measure of compensation or, more broadly, inadequate protection of the plaintiff’s performance interest, why should that not be addressed directly by improving the compensatory measure?

Chen-Wishart reasons that simply allowing disgorgement in particular cases where compensation is inadequate does not completely prevent this inadequacy from occurring in all cases. An injured party who has suffered no loss might receive a remedy where the party in breach has (perhaps fortuitously) made gains, but another might be left to the inadequacy of compensation because the party it contracted with did not profit (again, perhaps quite fortuitously) from the breach.<sup>89</sup> It seems intuitively unappealing that one party can receive an award of damages while another cannot, and that the basis of the award seems largely dependent on the actions of the party in breach, or even on chance. Disgorgement merely allows the injured party to switch from claiming a remedy based on its loss to one based on the gain of the party in breach.

Such an argument is attractive, but its downfall is evident in the lack of solutions provided by the critics of disgorgement. Claims to resolve the inadequacies of compensation by changes within the remedial scheme of

---

<sup>87</sup> Lecturer in Law at the University of Oxford.

<sup>88</sup> Chen-Wishart, *supra* note 81, 367.

<sup>89</sup> *Ibid* 367-368.

compensation have not been effectively supported by substantive suggestions for such changes.

An alternative approach is offered by Mitchell.<sup>90</sup> She argues that the inadequacy of compensatory damages for breach of contract “is not internal to the compensatory measure but is caused by contract law’s commitment to compensation as the presumptive remedy”.<sup>91</sup> The law of contract, in upholding compensation as its primary remedy, does not enforce the injured party’s right to performance, but its right to compensation upon breach.<sup>92</sup>

If this results in inadequate remedies, then the question must be whether the law of contract should recognise a right to performance in certain cases, or even at all. In other words, it is necessary to determine when a contract confers a legitimate interest in performance on a party, such that an order of specific performance would be justified.

The Court of Appeal in *Attorney-General v Blake* suggested two situations where a legitimate interest exists “in which justice requires the award of [disgorgement] ... where compensatory damages would be inadequate”.<sup>93</sup> The first is “skipped performance”.

Skipped performance occurs when “the defendant fails to provide the full extent of the services” that it has contracted to provide.<sup>94</sup> To determine whether there has been skipped performance, the injured party must have specified the particular type or level of service. Where the injured party has done this, it may be said that it has a legitimate interest in performance<sup>95</sup> or otherwise it would not have specified the performance.

Jaffey<sup>96</sup> criticises this first category because of its exclusion of other types of failure of performance that are no less wrongful than skipped performance. For example, he asks, why should skipped performance be treated more seriously than non-performance or defective performance?<sup>97</sup> On appeal to the House of Lords, Lord Nicholls also raised doubts as to

<sup>90</sup> Lecturer in Law at the University of Hull.

<sup>91</sup> Mitchell, “Remedial Inadequacy in Contract and the Role of Restitutionary Damages” (1999) 15 JCL 133, 150.

<sup>92</sup> Such an argument is based on the theoretical approach of Holmes. For the reasons given in Part V.1 and noting the distinction made between primary and secondary obligations of a contract (the primary obligation is to perform and the secondary obligation is to pay damages for the failure to perform), such an approach is doubtful. As to the distinction between primary and secondary obligations of a contract. See *supra* note 11, 651 per Lord Hobhouse.

<sup>93</sup> *Supra* note 1, 458.

<sup>94</sup> *Ibid.*

<sup>95</sup> Grantham and Rickett, *supra* note 11, 482; see also Virgo, *supra* note 8, 501-502.

<sup>96</sup> Senior Lecturer in Law at Brunel University.

<sup>97</sup> Jaffey, “Disgorgement for Breach of Contract and for a Criminal Offence” [1998] LMCLQ 469, 472.

the suggested categorisation, particularly where the consequences to the injured party of such a breach, which occurs often in contracts both for services and goods, are adequately resolved by compensatory measures. The injured party, having specified the required performance, can quantify its expectation interest where that performance does not occur.<sup>98</sup>

The second situation is where the defendant obtains its profit by doing the very thing that it contracted not to do. The objection to this category is obvious. “Arguably, *all* breaches of contract involve the defendant doing something he had contracted not to do, namely, depart from the contractual undertaking.”<sup>99</sup> In suggesting this category, Lord Woolf MR cited and approved the argument of Professor Birks<sup>100</sup> that disgorgement should be available where the breach was deliberate.<sup>101</sup> However, such a justification is in direct contradiction with the Court of Appeal’s refusal to allow disgorgement on the basis of moral culpability alone. Furthermore, the majority of the House of Lords has now ruled that something more than a mere breach is required before disgorgement will be justified.<sup>102</sup>

The Court of Appeal considered it desirable to extend the availability of disgorgement beyond proprietary rights to contracts where the injured party has a legitimate interest in performance. However, in doing so, it categorised as legitimate, interests that were subsequently shown both to be conceptually difficult and not sufficiently comprehensive.

## VII. ATTORNEY-GENERAL V BLAKE IN THE HOUSE OF LORDS

Following the decision in the Court of Appeal against the defendant on the public law claim, the defendant appealed to the House of Lords. On the initiative of the House of Lords, the issue of the availability of disgorgement was put before it for authoritative judicial statement.<sup>103</sup>

The House of Lords upheld the appeal on the public law claim, but ruled, by a majority of four to one, in favour of the availability of a remedy in disgorgement to strip the defendant of his profits.

The leading majority speech, given by Lord Nicholls, recognised the now well-accepted principle that the remedy of disgorgement is available

---

<sup>98</sup> Supra note 11, 639-640

<sup>99</sup> Chen-Wishart, supra note 81, 365, emphasis in the original

<sup>100</sup> Professor of Law at the University of Oxford

<sup>101</sup> See, for example, Birks, “Restitutionary Damages for Breach of Contract *Snepp* and the Fusion of Law and Equity” [1987] LMCLQ 421

<sup>102</sup> Supra note 11

<sup>103</sup> Ibid 644 per Lord Steyn

where a proprietary right is infringed.<sup>104</sup> It also discussed the distinctions in the remedial schemes adopted in equity and at common law, concluding that they “have arisen simply as an accident of history”<sup>105</sup> and are now only relevant as a matter of historical inquiry.

Acknowledging that compensation is inadequate in certain circumstances and that equitable remedies of specific performance and injunctions will not always be available, Lord Nicholls sought to determine whether disgorgement would nevertheless be available in such circumstances.

His Lordship readily accepted that damages in contract are not necessarily restricted to compensation of direct financial loss but can be measured by the benefit gained by the party in breach, resulting in a payment to the injured party of the reasonable price of that benefit, as in *Wrotham Park*. What was at issue was whether complete disgorgement, an “account of profits”, could ever be given as a remedy for breach.

No legal principle or explicit case law could be found either to support or deny the proposition, but Lord Nicholls ruled that, based on considerations of justice and fairness, the remedy of disgorgement must be available. His Lordship used jurisdictional arguments to support his conclusion.<sup>106</sup> His Lordship reasoned that if the court has power to grant the discretionary equitable remedies of injunction and specific performance for breach of contract, recognising that damages are not always a sufficient remedy, then such a power must surely extend to disgorgement where those equitable remedies cannot be granted. If the plaintiff’s interest in the performance of the contract renders it just and equitable that the defendant should retain no benefit from their breach of contract, the court must grant the plaintiff a remedy in disgorgement.

Further, it was noted that since an account of profits is an acceptable remedy for equitable wrongs, it would be anomalous if an account of profits could not also be given as a remedy for contractual wrongs.

Lord Nicholls acknowledged the uncertainty of a test based on a discretionary exercise of power where it would be just and equitable to do so. However, his Lordship did not believe that it would be so uncertain as to have an “unsettling effect on commercial contracts where certainty is important”.<sup>107</sup> Disgorgement would only be available in exceptional cases where compensatory and equitable remedies were inadequate.

---

<sup>104</sup> Ibid 632-633.

<sup>105</sup> Ibid 634.

<sup>106</sup> Ibid 638.

<sup>107</sup> Ibid 639.

The majority of their Lordships held that the availability of disgorgement could not be prescribed with fixed rules. Rather, the contractual terms and surrounding circumstances of each case must be considered, giving particular attention to whether the injured party has a legitimate interest in preventing the profit-making activity of the party in breach, and hence in the performance of the contract. As noted, the House of Lords regarded the Court of Appeal's attempts to define more specifically the categories of legitimate interests as difficult and unwise.

Lord Steyn, while in the majority and in general agreement with the reasoning of Lord Nicholls, gave a separate speech explaining the particular factors that he considered in determining that such a result was correct in principle.<sup>108</sup> His speech follows very similar reasoning, giving consideration to the terms of the contract itself and to the close analogy of the defendant's obligations with those of a fiduciary. His Lordship also stressed that the attainment of "practical justice" was a major objective of any judge.<sup>109</sup>

## 1. In the Interests of Justice and Fairness

Their Lordships were well aware that the apparent absence of conceptual clarity or theoretical foundations threatened the strength and legitimacy of their decision and, consequently, over-emphasised the attainment of the ideological principles of justice and fairness as the foundations of their conclusion.

Such weaknesses did not pass by unnoticed in the dissenting speech of Lord Hobhouse. His Lordship highlighted two difficulties in the majority decision, the first of which focussed on issues of justice and fairness. The "just response" that the majority was so keen to obtain was the punishment and deprivation of any fruits of the defendant's *criminal* conduct.<sup>110</sup> While the defendant was criminally liable, it was not appropriate to punish him using a cause of action founded in private commercial law. Criminal conduct is properly dealt with only in criminal law. The defendant had already been convicted for his criminal acts and the payment of royalties to Blake, which the Crown was attempting to prevent, did not amount to a criminal offence for which Blake could be prosecuted.

---

<sup>108</sup> Ibid 645.

<sup>109</sup> Ibid.

<sup>110</sup> Ibid 648-649.

Further, Lord Hobhouse warned that an extension in the availability of non-compensatory damages for breach of contract would result in “far reaching and disruptive” consequences for commercial law.<sup>111</sup>

## 2. Conceptual Frameworks of Restitution and Compensation

Lord Hobhouse’s second criticism was that the assumption that disgorgement is the correct remedy to “fill the gap” where compensation is inadequate is erroneous in light of both the concepts of restitution and compensation.<sup>112</sup>

Disgorgement, being restitutionary in nature,<sup>113</sup> is concerned with the unjust transfer of a plaintiff’s wealth or advantage to the defendant.<sup>114</sup> The most common forms of wealth in a restitutionary claim are property rights recognised in equity - such as those arising from a fiduciary relationship - and the truly restitutionary rights founded on unjust enrichment.<sup>115</sup> It is these rights that manifest a plaintiff’s legitimate interest in performance, which is generally enforced by equitable remedies. What is recovered is the wealth that the injured party is actually entitled to, which can be expressed in monetary terms. The objective of disgorgement is thus to *enforce* performance of the contractual obligations.

Compensation, on the other hand, is a *substitute* for performance. While it is used to place the injured party in the same position as if the contract had been performed, Lord Hobhouse noted that it is erroneous to “describe compensation as relating to a loss as if there has to be some identified physical or monetary loss” to the injured party.<sup>116</sup> The profit made by a party in breach can be evidence of the amount of the injured party’s loss.<sup>117</sup> This point was, interestingly, approved by Lord Nicholls, who stated that, where circumstances require, compensatory damages could be measured by reference to the benefit obtained by the wrongdoer.<sup>118</sup>

Lord Hobhouse held that the Crown did not have sufficiently substantive rights in the contract (proprietary rights) to amount to a

---

<sup>111</sup> Ibid 653

<sup>112</sup> Ibid 649

<sup>113</sup> See text supra Part II

<sup>114</sup> Supra note 11, 650 per Lord Hobhouse

<sup>115</sup> Ibid

<sup>116</sup> Ibid 651

<sup>117</sup> Waddams, supra note 59, 125, see also Stoljar, “Restitutionary Relief for Breach of Contract” (1989) 2 JCL 1, 12

<sup>118</sup> Supra note 11, 637 per Lord Nicholls, approving *Wrotham Park*

legitimate interest requiring the restitutionary remedy of disgorgement to be made. Consequently, the only available remedy was compensation, provided that the injured party could establish loss. His Lordship recognised that such a loss could be calculated as the sum that the injured party could have required of the breaching party as the price of its release from the contractual obligation.<sup>119</sup>

This extension of the conventional understanding of loss must surely be correct, for otherwise the interference with a party's (non-proprietary) contractual rights would amount to a power of compulsory acquisition of the injured party's contractual rights by the party in breach, without any payment in return.<sup>120</sup> The quantum of such a payment should be assessed by reference to the reasonable price for the release. This will usually be the market price but, where that possible measurement is absent, it is conceivable that the court would estimate a reasonable value on the basis of a hypothetical transaction,<sup>121</sup> which supposes an eager but not desperate seller.

In applying his preferred criteria for a remedy, Lord Hobhouse not only denied the Crown a remedy in disgorgement for want of any substantial right to support such a remedy, but further held that the Crown was ineligible for compensatory damages. While loss can be assessed by reference to the reasonable price of release, the information to which the defendant's contractual undertaking related was no longer confidential at the time of the breach of the obligation. Therefore, the defendant's contractual obligation not to disclose the information had no value to the Crown at the time of the breach.

### 3. Concluding Comments on *Attorney-General v Blake*

The reasoning of the majority relies too heavily on ideals of justice and fairness to the extent that existing principles of compensation and disgorgement are unnecessarily ignored. Such a rejection is unjustified because, upon application, these principles result in sufficient justice and fairness without disregarding the importance of the nature of the rights which the breached contract was originally created to protect. This is demonstrated in the proposed approach which, it is suggested, should be adopted in the determination of remedies for breach of contract.

---

<sup>119</sup> Ibid 652 per Lord Hobhouse.

<sup>120</sup> See O'Dair, *supra* note 22, 118-119.

<sup>121</sup> Waddams, *supra* note 59, 125.

## VIII. THE APPROPRIATE APPROACH TO REMEDIES FOR BREACH OF CONTRACT: A BLUEPRINT

Compensation is, in general, the primary and presumptive remedy for breach of contract. Although the measure of compensation is based on the actual loss of the injured party, defined as either the expectation or reliance interest, there is no real reason why the gains made by the party in breach, as a result of the breach, cannot be referred to when determining the injured party's true loss. Where the injured party can show that, had the party in breach requested a release from its contractual obligations, it would have consented to a reasonable price, the court should assign a market value to that price and award it as compensation. Such an award entails a more sophisticated understanding of the scope of the expectation interest for the purposes of compensation. The injured party is entitled to expect performance. Where the other party chooses not to perform, or to perform differently, without consent, the injured party could reasonably be said to expect a payment for the other party's release from the obligation to perform.

However, where the injured party has a legitimate interest in performance, evidenced by the existence of proprietary rights arising out of the contract, compensation will be an inadequate remedy for a breach of contract. In such a case, the principles of equitable remedies and restitution apply. Where it is not possible to grant an equitable remedy, for instance where the breach cannot be reversed, or where it is inappropriate to grant such a remedy, for instance, where such a remedy would result in an "unpardonable waste" as in *Wrotham Park*, disgorgement of the breaching party's profits should be granted to vindicate the injured party's proprietary rights. The remedy of disgorgement should require an account of *all* profits because of the distinct nature of proprietary rights. The party in breach has derived a profit from some thing or asset that belonged to the injured party.<sup>122</sup>

The most obvious objection to this proposal, that this would result in a windfall to the injured party, is based on the failure to recognise the fundamental protection accorded to proprietary rights in our system of law. Critics argue that a restitutionary response applies only to reverse a wrongful transfer of wealth from the injured party to the party in breach and that in cases of breach of contract, the party in breach has made a

---

<sup>122</sup> Ibid 121.

profit that did not originally belong to the injured party. Thus, awarding that profit to the injured party is not a return of its property but a windfall that it would never have otherwise received.<sup>123</sup>

However, it is not the ownership of the profit that is at issue, but the ownership of the proprietary right in respect of the asset from which the profit derived. The injured party, because of its ownership in that asset, has the right not to have it interfered with. The breaching party's actions, in deriving a profit from the use of the asset, are a direct interference with the injured party's property rights and amounts, therefore, to a wrong committed against it in respect of its ownership of the thing.<sup>124</sup> The party in breach must be held accountable for this wrong. It is an act that must trigger legal consequences because it is an interference with the injured party's proprietary rights.

It is not appropriate, in formulating the correct approach to the availability of disgorgement, to take into account theories of economic efficiency unless the presumptions on which these theories are based are well understood and followed consistently in their application. As has been argued, when the presumptions are correctly followed, the arguments of economic efficiency show that allowing disgorgement does not result in any negative consequences that are not already present within a purely compensatory remedial scheme.

Further, it is considered that to drastically alter the remedial scheme of contract law, as the majority of the House of Lords in *Attorney-General v Blake* appeared to be willing to do, is highly unnecessary where "the principle of compensation is both intellectually sound as the remedy for breach and provides the just answer".<sup>125</sup> The complaint that compensation is inadequate is unjustified. A comprehensive analysis of the compensatory scheme shows that the expectation interest can include the expectation of the value of release in the event of breach. It is only where the breach of contract amounts to an interference with proprietary rights that the expectation value of a release of the obligation to perform is not an adequate remedy. This situation must be corrected by imposing well-defined principles of disgorgement.

To resort to reasons of justice and fairness determined on an ad hoc basis, as the majority in *Attorney-General v Blake* did, is unnecessary where principled remedial schemes already exist. It is also undesirable because of the uncertainty it creates in the determination of remedies and

---

<sup>123</sup> Edelman, "Restitutionary Damages and Disgorgement Damages for Breach of Contract" [2000] RLR 129, 150-151.

<sup>124</sup> Grantham and Rickett, *supra* note 11, 469.

<sup>125</sup> *Supra* note 11, 653 per Lord Hobhouse.

the disruptive and unsettling effect this has on the practice of contracting, particularly in a commercial context where certainty as to the law and, hence its reliability, are highly prized values.