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## A Relational Critique of the Third Restatement of Restitution § 39

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# A Relational Critique of the Third Restatement of Restitution § 39

David Campbell\*

## *Abstract*

*In the Restatement (Third) of Restitution and Unjust Enrichment, breach of contract is regarded as a "wrong," and, in response to the perceived shortcomings of the current law of remedies based on compensatory damages, the proposed Section 39 seeks to provide for disgorgement of profit as an alternative remedy for "opportunistic" breach. In so doing, the Restatement is substantially repeating the argument for the extension of restitutionary remedies for breach of contract which recently has had great success in the Commonwealth. The restitutionary criticism of compensatory damages is, at root, that those damages are unable to prevent important forms of immoral or amoral contracting behaviour. However, this Article argues that, viewed from the perspective of the relational theory of contract, compensatory damages encourage a valuably cooperative attitude towards dealing with problems which arise in the course of contracting, and that Section 39 would undermine that attitude, diminishing the moral quality of contracting.*

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\* Professor of International Business Law, School of Law, University of Leeds, U.K. The idea of this Article arose whilst I held a Visiting Professorship at Cardozo Law School, New York in 2008–2009. I should like to thank Cardozo for its hospitality, and the students of the Advanced Contracts class I taught there for their stimulating questions about the topic of this Article. Early versions of the paper were given to the Wisconsin Law School Contracts Group and to the Contracts and Commercial Law Section of the Society of Legal Scholars, U.K. I am grateful for comments given at these readings. I also should like to thank Richard Austen-Baker, James Devenney, Jay Feinman, Peter Goodrich, John Kidwell, Andrew Kull, Stewart Macaulay, Paul Shupack, and Bill Whitford for particularly generous help.

This Article is dedicated to the memory of Ian Macneil, who died on Tuesday 16 February, 2010, in gratitude for the great kindness Ian showed the present author over 25 years.

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### I. Introduction

In the Restatement (Third) of Restitution and Unjust Enrichment (R3RUE),<sup>1</sup> breach of contract is regarded as a "wrong," and in response to certain perceived shortcomings of the current law of remedies based on compensation of lost expectation, the proposed Section 39 seeks to extend restitution to provide for disgorgement of profit as an alternative to compensatory damages in cases of "opportunistic breach." In so doing, R3RUE is substantially repeating the argument for the extension of restitutionary remedies for breach of contract which has had considerable success in the Commonwealth since the appearance of Goff and Jones' *The Law of Restitution* in 1966<sup>2</sup> and Birks's *An Introduction to the Law of*

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1. RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT (2011) [hereinafter R3RUE]. As this Article was written, R3RUE was set out in six Tentative Drafts, between April 6, 2001 and March 12, 2008. A concluding, seventh tentative draft appeared on March 12, 2010, on which see *infra* note 11.

2. See ROBERT GOFF & GARETH JONES, *THE LAW OF RESTITUTION* 521–22 (7th ed. 2007) ("[C]ourts have not taken too kindly to opportunistic breach of contract. Their readiness to strip the party in breach of his profits had to be concealed as an award of damages. There is evidence that judges have become impatient with such fictions." (citations omitted)).

*Restitution* in 1985.<sup>3</sup> Such has been the importance of the late Professor Peter Birks in making this argument that I propose to call it the Birksian argument, though this somewhat misdescribes Birks's own interests, which were never focused on contract, and is quite unfair to the contract scholarship of Lord Goff, Professor Jones and many other contributors.<sup>4</sup> The Birksian argument was gradually acknowledged in a number of cases following *Wrotham Park Estate Co. Ltd. v. Parkside Homes Ltd.* in 1974,<sup>5</sup> and authoritatively endorsed by the, in terms of the formal law of damages, revolutionary House of Lords's decision in *Attorney General v. Blake (Jonathan Cape Third Party)* in 2001.<sup>6</sup>

I have strongly criticised this development in the law of England and Wales,<sup>7</sup> and this Article is written to bring this criticism to the attention of a U.S. audience which has "widely applauded" Section 39.<sup>8</sup> I by no means

3. See PETER BIRKS, AN INTRODUCTION TO THE LAW OF RESTITUTION 3 (rev. ed. 1989) ("[T]his book is pre-occupied with the task of finding the simplest structure on which the material in *Goff and Jones* can hang.").

4. In his comments on the draft of this Article, Professor Kull has rightly pointed to the way that many fundamentals of the Birksian argument were anticipated in the work of Seavey and Scott, the Reporters of the first Restatement. As Kull is perfectly well aware, in the British literature this point has been raised in criticism of Birks, who never engaged with the Restatement in any real depth. See Andrew Kull, *James Barr Ames and the Early Modern History of Unjust Enrichment*, 25 OXFORD J. LEGAL STUD. 297, 298 n.2 (2005) ("A restitution skeptic like Steve Hedley is similarly content to let the American Law Institute take the credit—such as it is—for originating what he calls 'the current view of the subject.'" (citing STEVE HEDLEY, A CRITICAL INTRODUCTION TO RESTITUTION 8–9 (2001))). Birks's most substantial, if this is the right word, comment on the Restatement was to criticise Seavey and Scott, as he criticised everyone who had written on these matters prior to himself, for adhering to "the tripartite division of the law into contract, tort and restitution." Peter Birks, *Unjust Enrichment and Wrongful Enrichment*, 79 TEX. L. REV. 1767, 1769 (2001) (quoting Warren A. Seavey & Austin W. Scott, *Restitution*, 54 LAW Q. REV. 29, 31 (1938)); see also Peter Birks, *A Letter to America: The New Restatement of Restitution*, 3(2) GLOBAL JURIST FRONTIERS art. 2 (2003) available at <http://www.bepress.com/gj/frontiers/vol3/iss2/art2> ("Intoxicating as the restitution excitement has been, it has from the outset been seriously flawed. The evidence of the flaw is that the passage of 70 years has not reconciled the common law to the simple classification of the causative events which was introduced above . . ."). On the specific point of "subtraction," see *infra* Part IV.

5. See *Wrotham Park Estate Co. v. Parkside Homes Ltd.*, [1974] 1 W.L.R. 798 (Ch.D.) (allowing for the recovery of 5% of the builder's profits from the development of land subject to a restrictive covenant not to develop).

6. See *Attorney Gen. v. Blake*, [1997] Ch. 84 (Ch.D.); [1998] Ch. 439 (C.A.); [2001] 1 A.C. 268 (H.L.(E.)) (finding that an accounting for of profits was an appropriate remedy for a former English Secret Intelligence Service member who wrote a book about his experiences in the Service without first obtaining permission as required by contract).

7. I should make it clear that my thoughts on this subject have been formed in close collaboration with a number of coauthors who are identified in citations *infra*.

8. James S. Rogers, *Restitution for Wrongs and the Restatement (Third) of the Law of*

wish to recapitulate all of this criticism but, rather, to focus on the, in my opinion, simple issue that underlies the labyrinthine twists and turns taken by the treatment of breach of contract in the Birksian argument. This issue is whether the effective general permission of breach in the expectation-based law of remedies is a good policy. The Birksian argument has been driven by a belief that it is not, indeed that it is seriously mistaken and gives rise to immoral or amoral contracting behaviour. This has led to arguments that a stronger remedy which will more effectively prevent breach is needed; that restitutionary damages are such a remedy; and that the wider availability of these damages will buttress the moral quality of the law of contract.

The U.S. discussion is fortunate in that the excellent Comments and Notes produced by the Reporter, Professor Andrew Kull of Boston University School of Law, show that the argument for Section 39 is ultimately concerned, not with abstract ratiocination,<sup>9</sup> but with the practical contribution Section 39 will make towards reinforcing "the stability of . . . contract itself."<sup>10</sup> The contrast with much of the Commonwealth discussion is marked. In three valuable papers,<sup>11</sup> Professor Caprice Roberts of West Virginia University has examined what I believe is the issue on which the "stability of contract" turns: the morality of breach.<sup>12</sup> She discusses with

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*Restitution and Unjust Enrichment*, 42 WAKE FOREST L. REV. 55, 66 (2007).

9. I will mention, without detailed discussion, that on a number of occasions Professor Kull has simply dismissed as "arid," or some synonym of arid, a number of abstract talking points that have been thought to be of absorbing interest in the Commonwealth debate.

10. RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39 cmt. b (2011).

11. I am afraid that serious illness prevented me from attending the symposium or reading the contributions prior to the deadline for submission of this Article, so I have been unable to make detailed reference to those contributions, including that of Professor Roberts. For this reason, I was also unable to consider the seventh Tentative Draft, but have since confirmed that it did not necessitate any alteration of my argument.

12. See generally Caprice Roberts, *A Commonwealth of Perspective on Restitutionary Disgorgement for Breach of Contract*, 65 WASH. & LEE L. REV. 945 (2008) [hereinafter Roberts, *Commonwealth of Perspective*]; Caprice Roberts, *Restitutionary Disgorgement for Opportunistic Breach of Contract and Mitigation of Damages*, 42 LOY. L.A. L. REV. 131 (2008) [hereinafter Roberts, *Restitutionary Disgorgement*]; Caprice Roberts, *Restitutionary Disgorgement as a Moral Compass for Breach of Contract*, 77 U. CIN. L. REV. 991 (2009) [hereinafter Roberts, *Moral Compass*].

Roberts takes up a theme that has had only vestigial treatment in the Commonwealth discussion. See, e.g., I.M. Jackman, *Restitution for Wrongs*, 1989 CAMBRIDGE L.J. 302, 302 ("In what circumstances can a person be liable to a pecuniary remedy for conduct which has not caused the plaintiff any harm? This question lies at the heart of the present topic . . ."). She argues that enforceability is necessary for the institution of contract to work. I am sure

skill certain relatively narrow points of remedies doctrine which undoubtedly arise in connection with § 39, but which I will largely ignore. However, she rightly puts this discussion in the context of the law of mitigation, and she, even more rightly, relates all of this to the ethical foundations of contract. By doing so, she has provided the opportunity for the U.S. discussion of restitutionary remedies for breach of contract to be conducted on a sounder footing than it has enjoyed for most of the time in the Commonwealth.<sup>13</sup>

She is, however, in my opinion, wrong to think that expectation-based remedies do not institutionalize a moral position. They do. It is a position in which parties are encouraged to cooperate to deal with the consequences of breach. This is, in fact, a far superior moral position to that which would be established by the wider availability of restitutionary damages, which would give an unbalanced and indefensible power to the plaintiff to vindicate his formal rights, and so deny the ethic of cooperation at the heart of the expectation-based law of remedies. I write, however, in the conditional tense, for the wider availability of restitutionary damages so conflicts with freedom of contract that it cannot be established without extinguishing that freedom, and so, in my opinion, it has no chance whatsoever of becoming settled law.

My argument amounts to a defense of the expectation-based law of remedies. I do not, however, wish to defend the conventional, (neo)classical,<sup>14</sup> understanding of that law, of which I am profoundly

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she is right, but this does not mean that enforceability need be of the literal sort she envisages. I do not want to go into the issue at all, but it is incumbent upon Roberts to address the way that Durkheim, whose views are central to the discussion of this matter, emphasizes that the modern form of solidarity is flexibly "organic" rather than rigidly "mechanical," and, in my opinion, Durkheim's account of modern solidarity readily embraces the flexibility I will argue is brought to the law of remedies by compensatory damages. EMILE DURKHEIM, *THE DIVISION OF LABOUR IN SOCIETY* 149–78 (1984). An excellent discussion of the issue within the legal literature is J.H. Gebhardt, *Pacta Sunt Servanda*, 10 MOD. L. REV. 159 (1947).

13. A rare example of contribution to the Commonwealth literature which focused on the effect of *Blake* on the practical operation of commercial law is Gillian Black, *A New Experience in Contract Damages? Reflections on Experience Hendrix v PPX Enter.*, 2005 JURID. REV. 31. I responded to Ms. Black's paper in David Campbell, *The Defence of Breach and the Policy of Performance*, 25 U. QUEENSLAND L.J. 271 (2006).

14. I follow Ian Macneil's distinction of classical and neo-classical conventional contract thinking. See Ian R. Macneil, *Contracts: Adjustment of Long-term Economic Relations Under Classical, Neo-Classical and Relational Contract Law*, 72 NW. U. L. REV. 854, 855 n.2 (1978) ("Classical contract law refers . . . to that developed in the 19th century and brought to its pinnacle . . . in the RESTATEMENT OF CONTRACTS (1932). Neoclassical contract law refers to a body of contract law founded on that system in overall structure but

critical.<sup>15</sup> I write from the intrinsically ethical perspective of the relational theory of contract, to which I have sought to contribute for twenty-five years, and my argument shares Roberts's concern with the moral nature of contract.

## II. Section 39 and the Impulse Behind Restitutionary Remedies for Breach

Headed "Profit Derived from Opportunistic Breach," Section 39 reads:

1. If a breach of contract is both material and opportunistic, the injured promisee has a claim in restitution to the profit realized by the defaulting promisor as a result of the breach. Liability in restitution with disgorgement of profit is an alternative to liability for contract damages measured by injury to the promisee.
2. A breach is "opportunistic" if
  - a) the breach is deliberate;
  - b) the breach is profitable by the test of subsection (3); and
  - c) the promisee's right to recover damages for the breach affords inadequate protection to the promisee's contractual entitlement. In determining the adequacy of damages for this purpose,
    - (i) damages are ordinarily an adequate remedy if they can be used to acquire a full equivalent to the promised performance in a substitute transaction; and
    - (ii) damages are ordinarily an inadequate remedy if they cannot be used to acquire a full equivalent to the promised performance in a substitute transaction.
3. A breach is "profitable" when it results in gains to the defaulting promisor (net of potential liability in damages) greater than the promisor would have realized from performance of the contract. Profits from breach include saved expenditure and consequential gains that the defaulting promisor would not have realized but for the breach. The

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considerably modifies in some . . . of its detail.").

15. See generally David Campbell, *The Undeath of Contract*, 22 HONG KONG L.J. 20 (1992).

amount of such profits must be proved with reasonable certainty.<sup>16</sup>

A (material) breach is, then, "opportunistic" when it is "deliberate," "profitable," and "the promisee's right to recover damages for the breach affords inadequate protection to the promisee's contractual entitlement." The impulse behind this section, as in the development of the restitutionary remedy in England and Wales, was the perception that expectation-based damages can leave the plaintiff inadequately protected against profitable breach, and that defendants will take advantage of this opportunity profitably to breach.

As is pointed out in R3RUE,<sup>17</sup> and as is dwelt on by Roberts in all three of her papers, Section 39 will have important implications for the concept of "efficient breach." I will argue that Kull's and Roberts's criticisms of this vexed concept are somewhat ill-directed, but their understanding perfectly fairly reflects the dominant treatment of it in contract scholarship, which is, of course, derived from Posnerian law and economics. Kull rightly tells us that in discussions of efficient breach, "it is suggested" that "[t]he seller . . . ought to breach the contract whenever the anticipated profits from resale at the higher price would be more than sufficient to pay the buyer's damages, thereby leaving some parties better off and nobody worse off."<sup>18</sup> Ensuring that "a person is not permitted to profit by his own wrong" is one of the general principles of R3RUE,<sup>19</sup> and it is clear from the general discussion of restitution for wrongs that what is at issue in Section 39 ultimately<sup>20</sup> is a moral issue turning on this

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16. RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39 (Tentative Draft No. 4, 2005). A subsection 4 adds:

Disgorgement by the rule of this Section will be denied: (a) if the parties' agreement authorizes the promisor to choose between performance of the contract and a remedial alternative such as payment of liquidated damages; or (b) to the extent that disgorgement would result in an inappropriate windfall to the promisee, or would otherwise be inequitable in a particular case.

*Id.* Kull's substantial argument in earlier academic work stated, "[d]isgorgement awarding the plaintiff more than he lost is justified in a narrow class of cases in which the defendant's election to breach imposes harms that a potential liability for provable damages will not adequately deter." Andrew Kull, *Disgorgement for Breach, the Restitution Interest and the Restatement of Contracts*, 79 TEX. L. REV. 2021, 2052 (2001).

17. See RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39 cmt. h (2011) ("The rationale of the disgorgement liability in restitution, in a contractual context or any other, is inherently at odds with the idea of efficient breach in its usual connotation.").

18. *Id.*

19. *Id.* § 3.

20. See, e.g., *id.* § 3 cmt. c ("Restitution requires full disgorgement of profit by a



principle.<sup>21</sup> Roberts provides some highly interesting amplification of this aspect of the thinking behind Section 39.<sup>22</sup>

Though, to my knowledge, the term efficient breach was coined as late as 1977<sup>23</sup> and the first formal statement of the concept was made only in 1970,<sup>24</sup> the concept is traceable to Holmes's famous observation that "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. [The law of contract] leaves [the promisor] free to break his contract if he chooses."<sup>25</sup> This "option" or "choice" theory of contractual obligation is found objectionable by Kull and by Roberts, and by many, many others of course, including, I have no doubt, the other contributors to this symposium,<sup>26</sup> because it articulates what is regarded as the amoral attitude

conscious wrongdoer, not just because of the moral judgment implicit in the rule of this section, but because any lesser liability would provide an inadequate incentive to lawful behavior.").

21. See, e.g., *id.* § 39 cmt. b ("In countering this form of opportunism, the rule of Section 39 reinforces the contractual position of the vulnerable party and condemns a form of conscious advantage-taking that is the equivalent, in the contractual context, of an intentional and profitable tort.").

22. See, e.g., Roberts, *Moral Compass*, *supra* note 12, at 992 ("To say that we are morally obligated to keep our promises means precisely that: that we are obligated. The promise imposes an imperative from an earlier to a later self to be obeyed, not an option to be weighed.").

23. See Charles J. Goetz & Robert E. Scott, *Liquidated Damages, Penalties and the Just Compensation Principle: Some Notes on an Enforcement Model and a Theory of Efficient Breach*, 77 COLUM. L. REV. 554, 558 (1977) ("[M]odern . . . contract damages [are] based on the premise that a contractual obligation is not necessarily an obligation to perform, but rather an obligation to choose between performance and compensatory damages. . . . As long as the compensation adequately mirrors the value of performance, this damage rule is 'efficient.'" (citations omitted)).

24. See Robert Birmingham, *Breach of Contract, Damage Measures, and Economic Efficiency*, 24 RUTGERS L. REV. 273, 284 (1970) ("Repudiation of obligations should be encouraged where the promisor is able to profit from his default after placing his promisee in as good a position as he would have occupied had performance been rendered. . . . To penalize such adjustments. . . is to discourage efficient reallocation of community resources.").

25. OLIVER W. HOLMES, *THE COMMON LAW* 301 (1881).

26. From within the relational perspective see Ian R. Macneil, *A Primer of Contract Planning*, 48 S. CAL. L. REV. 627, 692 (1975) ("Inevitably the contract's contents are no longer the same once mutuality of exchange motivations has disappeared, since the most important single element of a viable ongoing contractual relationship commonly is the mutual desire to make it succeed."); and from within a more orthodox perspective (though sympathetic to the relational theory) see Joseph M. Perillo, *Misreading Oliver Wendell Holmes on Efficient Breach and Tortious Interference*, 68 FORDHAM L. REV. 1085, 1091 (2000) ("The linkage between efficient breach theory and the misunderstanding of Holmes's theory is finding its way into the courts, albeit in fairly innocuous ways thus far. It is likely,

of "the bad man,"<sup>27</sup> the expression in legal theory of the orientation of the economic rational individual utility maximizer at the heart of Posnerian law and economics. The *locus classicus* of this amoral attitude is Judge Posner's treatment of efficient breach in his extraordinarily successful textbook,<sup>28</sup> which surely has been the principal medium through which the concept has been brought to such prominence. In contrast to this, Roberts sees the greater assurance of a substantial remedy for breach, and therefore greater assurance of performance, provided by Section 39 as an important part of the moral compass which restitution can offer to contract, which expectation-based remedies, derived from Holmes, sadly lack.<sup>29</sup> Section 39, she tells us, involves a "significant" "intellectual shift" "in rationale" for remedies for breach which

will inject moral blameworthiness into contractual legal obligation. It will honor the view that one's word is one's bond . . . . It will send Holmesian-influenced contract teaching and lawmaking into a new period of introspection and, perhaps, revision. It will fuel efforts to dismantle efficient breach theory. It will resonate with moral instincts of some students, lawyers, and judges. It will deter. It will judge moral culpability. It will feel like punishment. It will ripple through contract law and related legal and business sectors.<sup>30</sup>

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however, to have the pernicious effect of encouraging the adoption of the efficient breach fallacy into the legal arena." (citations omitted)). For the reason set out *supra* note 11, I have been unable to make detailed reference to Professor Perillo's contribution to this symposium, or other relevant contributions.

27. Oliver W. Holmes, *The Path of the Law*, 10 HARV. L. REV. 457, 459 (1897).

28. See RICHARD POSNER, *ECONOMIC ANALYSIS OF LAW* 120 (7th ed. 2007) ("He will [breach] if the profit would also exceed the expected profit to the other party from completion of the contract, and hence the damages from breach. So in this case awarding damages will not deter a breach of contract. It should not. It is an efficient breach."). Though I will not describe this development here, Judge Posner's treatment of efficient breach has grown somewhat more sophisticated over successive editions of his textbook, and it is no longer, in fact, directly open to the criticisms typically made of it in the way it was in early editions.

29. See, e.g., Roberts, *Moral Compass*, *supra* note 12, at 1018 ("The new Restatement's doctrinalization of disgorgement (in the rare moment of opportunistic breach) may simply right the ship and recalibrate our understanding of what was already happening, reconcile the results, and incorporate common sense.").

30. *Id.* at 1026.

*III. What Some English Cases Tell Us Will Be the Problems with  
Section 39*

As Roberts says in her discussion of the Commonwealth case law and secondary literature,<sup>31</sup> this essentially is the argument that has been made for the extension of what are now called restitutionary damages in the law of England and Wales, which reached its high point in *Blake*. I have described the process by which these damages have come to be available in somewhat greater detail than Roberts,<sup>32</sup> but much of that detail can be of little use to the U.S. contract scholar, as opposed to the specialist in equity or restitution, or, indeed, the legal historian of these doctrines, and for present purposes there is no point of significant difference between my account and Roberts's account of the position established by *Blake*.

One point of clarification must, however, be made, if only to be put to one side. We will see that the Court of Appeal and the House of Lords were very anxious to keep *Blake* within narrow confines. One of the confines that was accepted was that *Blake* should not normally prevent efficient breach. This is said in so many words by both courts,<sup>33</sup> where desperate efforts were made to insulate the leading British case authorizing efficient breach, *Teacher v. Calder*,<sup>34</sup> from the effects of *Blake*. But this

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31. See Roberts, *Commonwealth of Perspective*, *supra* note 12, at 954–65 (detailing the adoption of disgorgement in *Blake* for the U.K. and noting its possible adoption in several other countries).

32. See generally DONALD HARRIS ET AL., REMEDIES IN CONTRACT AND TORT ch. 17 (2d ed. 2001); David Campbell & Donald Harris, *In Defence of Breach: A Critique of Restitution and the Performance Interest*, 22 LEGAL STUD. 208 (2002); David Campbell & Phillip Wylie, *Ain't No Telling (Which Circumstances Are Exceptional)*, 62 CAMBRIDGE L.J. 605 (2003).

33. See *Attorney Gen. v. Blake*, [1998] Ch. 439 (C.A.) 459 ("[I]t appears to us that the general rule that damages for breach of contract are compensatory can safely be maintained without denying the availability of restitutionary damages in exceptional cases."); *Attorney General v. Blake*, [2001] 1 A.C. 268 (H.L.(E.)) 286 (stating situations in which disgorgement would not be appropriate). The court stated:

[The lower court] suggested three facts which should not be a sufficient ground for departing from the normal basis on which damages are awarded: the fact that the breach was cynical and deliberate; the fact that the breach enabled the defendant to enter into a more profitable contract elsewhere; and the fact that by entering into a new and more profitable contract the defendant put it out of his power to perform his contract with the plaintiff. I agree that none of these facts would be, by itself, a good reason for ordering an account of profits.

*Id.*

34. See *Teacher v. Calder*, (1898) 25 R. 661 (finding that the plaintiff was not entitled to the defendant's profits, which the defendant had acquired by using the plaintiff's money in a distillery business as opposed to a timber business as called for in the contract), *aff'd* on

can, as I have said, be put to one side, because this defence of efficient breach is mere wishful thinking, in fact much more wishful than thoughtful, for there can be no doubt that the *Blake* doctrine does work against efficient breach. I have discussed this elsewhere, and refer the reader to that discussion,<sup>35</sup> and to a, very exceptionally reported, arbitration award by a highly distinguished panel subsequent to *Blake* which was intended to ram the point home.<sup>36</sup> Though Roberts should really have dealt with this attempt to reconcile *Blake* and efficient breach, which surely is somewhat awkward for her, I am sure that she captures the logic of the restitutionary remedy, in respect of this matter, better than have the highest English courts.<sup>37</sup>

But where, with respect, Roberts may be thought to be remiss is that she does not discuss in sufficient detail other English cases after *Blake* in which the attempt to turn the wider availability of restitutionary remedies into workable law has proven very problematic. Roberts perceptively anticipates the difficulties to which Section 39 will give rise,<sup>38</sup> but she does not deal with the cases in which these difficulties have already become manifest. The electronic databases tell us that *Blake* has been cited over 100 times in subsequent cases, and, whilst by no means are all of these on contract, and whilst not all of those on contract have a bearing on the general principles of contractual remedies, there are a number, some of which have reached the Court of Appeal, which demand serious discussion in this connection.<sup>39</sup>

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this point [1899] A.C. 451, 462, 467 (H.L.(SC.)).

35. See generally David Campbell, *The Treatment of Teacher v Calder in AG v Blake*, 65 MOD. L. REV. 256 (2002).

36. See AB Corp. v. CD Co. (*The Sine Nomine*), [2002] 1 LLOYD'S REP. 805, 806 (stating that in an exceptional case a plaintiff may "obtain wrongful profits as damages for breach of contract," but that on the facts in this case, an efficient breach did not require disgorgement); see also Campbell & Wylie, *supra* note 32, at 614–15 (discussing *The Sine Nomine*).

37. Roberts generously comments on some of the Commonwealth scholarship that has dealt more clearly with the implications of restitution for efficient breach. E.g., Roberts, *Commonwealth of Perspective*, *supra* note 12, at 968–77.

38. See, e.g., *id.* at 965 ("[T]he text of the proposed section is clunky and unappealing. . . . All of this unwieldiness seems calculated to avoid unnecessary association with the specific performance doctrine and to reassure those who are apprehensive that this section will be a slippery slope towards the perceived unbounded nature of tort remedies.").

39. The most authoritative review of the English law is HARVEY MCGREGOR, DAMAGES ch. 12 (18th ed. 2009). The version of this chapter in 17th ed. 2003 is still of value.

The point stressed by Kull<sup>40</sup> and by Roberts<sup>41</sup> is that restitutionary damages under Section 39 are to have a limited scope. Kull tells us that the definition of opportunistic breach "will exclude the vast majority of contractual defaults," and so Section 39 will be an "exceptional . . . claim."<sup>42</sup> Roberts seems rather to regret this at one level, but, of course it is necessary, as both she and Kull are acutely aware.<sup>43</sup> Were restitutionary damages available as an alternative to expectation-based damages for every breach, the law of contract would be changed in, to put it at its mildest, an utterly chaotic manner. This was pointed out by the late Lord Hobhouse in his formidable dissent in *Blake* itself.<sup>44</sup> The acceptability of restitutionary damages requires them to be, at the moment, restricted. Subsequent case law may well enlarge them, as Roberts certainly wants, and as most academic commentators on the issues in the Commonwealth want. But, at the moment, in the law of England and Wales, restitutionary damages are available only in, as it was put in *Blake*, "exceptional circumstances,"<sup>45</sup> and when I repeatedly have argued that they will not be able to be confined to these exceptional circumstances, it has been urged against me that the House of Lords wants them to be.<sup>46</sup> I am afraid I do not find this the most

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40. RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39 cmt. d (Tentative Draft No. 4, 2005) ("The first two elements of the definition—requiring that a breach be both deliberate and profitable—will serve in practice to exclude most contractual defaults . . .").

41. *E.g.*, Roberts, *Commonwealth of Perspective*, *supra* note 12, at 961–67 ("The inadequacy hurdle, although poorly drafted, is a significant hurdle to a plaintiff's obtaining (*not seeking*) disgorgement relief. In essence, if plaintiff could establish a right to specific performance by meeting the standard irreparable injury test, then plaintiff should have the option of seeking disgorgement.").

42. RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39 cmt. f (2011).

43. *See, e.g.*, Roberts, *Commonwealth of Perspective*, *supra* note 12, at 963 ("The requirement that the breach be 'profitable,' however, raises a formidable hurdle to disgorgement relief. In Professor Kull's estimation, truly profitable breaches are rare.").

44. *See* Attorney Gen. v. *Blake*, [2001] 1 A.C. 268 (H.L.(E.)) 299 ("I must also sound a further note of warning that if some more extensive principle of awarding non-compensatory damages for breach of contract is to be introduced into our commercial law the consequences will be very far reaching and disruptive.").

45. *Id.* at 285.

46. *See* ANDREW S. BURROWS, *THE LAW OF RESTITUTION* 486 n.18 (2d ed. 2002) ("Campbell and Harris . . . are highly critical of the reasoning in *Blake*: but their argument is directed against restitution for breach of contract as a generally-available remedy, whereas the House of Lords stressed that it should be an exceptional remedy only."); Ewan McKendrick, *Breach of Contract, Restitution for Wrongs, and Punishment*, in *COMMERCIAL REMEDIES* 93, 105, 105 n.68 (Andrew S. Burrows & Edwin Peel eds., 2003) ("[Accounting for profits for breach of contract] is a remedy of last resort and not, as some commentators appear to think, a remedy of primary resort." (citing Campbell & Harris, *supra* note 32)).

convincing reply, for the point is not what the House of Lords wants; the point is what it will get. And the cases so far show no ability whatsoever to draw a justiciable line between ordinary and exceptional circumstances.

It is, I think, clear that "deliberate" is not really the correct word to describe what is being aimed at in Section 39. As I will argue,<sup>47</sup> deliberation itself is neither here nor there, and it is only when one has the background belief that to breach a contract is a wrong in a more than technical sense that deliberate breach carries some pejorative implication in itself. In the United States, describing a breach as "wilfull" perhaps most effectively conveys the sense being sought, though "wilfull" thereby runs the risk of being a mere tautology for "opportunistic," to the extent that one can say that there can be a tautology composed of two terms both of which have proven radically difficult to define clearly. The most influential English equivalent to "wilfull" is that a breach is "deliberate and cynical,"<sup>48</sup> which obviously adds some conception of "the defendant's moral culpability"<sup>49</sup> to the notion of mere deliberation, perhaps better capturing the idea that there is something aggravating about "the moral calibre of the defendant's conduct"<sup>50</sup> which makes it morally inferior to the conduct of the "innocent" plaintiff.

But a breach being deliberate and cynical was never thought enough in itself even by the Court of Appeal in *Blake, inter alia* because "the line cannot easily be drawn in practise,"<sup>51</sup> and to it was added the grounds of "skipped performance"<sup>52</sup> and "doing the very thing which [the defendant] contracted not to do."<sup>53</sup> I have criticized these very flimsy grounds elsewhere,<sup>54</sup> but the point need not be pressed because they actually were abandoned in *Blake* itself, somewhere between the Court of Appeal's and

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47. See *infra* note 161 and accompanying text (discussing what is meant by "deliberate").

48. Attorney Gen. v. Blake, [1998] Ch. 439 (C.A.) 457.

49. *Id.*

50. *Id.* at 456.

51. *Id.* at 457.

52. *Id.* at 458.

53. *Id.*

54. See Campbell & Harris, *supra* note 32, at 228–30 (arguing that skipped performance and doing that which was contracted not to do, are inadequate bases for the accounting of profits remedy because absolute performance or liquidated damages can be negotiated for *ex ante*, and thereby priced into the contract). The Court of Appeal based the skipped performance ground on the famous case of *City of New Orleans v. Firemen's Charitable Assoc.*, 9 So. 486 (La. 1891). See also discussion *infra* Part VIII (discussing why disgorgement cases arise and how to deal with them).

the House of Lords's hearing of the case.<sup>55</sup> However, to say they were abandoned is misleading. Any attempt to state them as defensibly coherent legal concepts was abandoned, but the vague sentiment behind them was retained, and indeed has guided the case law after *Blake*. But not only is it impossible to see precisely what was meant by "deliberate" or "cynical" or some combination thereof in *Blake* itself, the attempt to sustain *any* such idea after *Blake* laughably collapsed when the Court of Appeal, in the most important decision since *Blake*, ended up protecting rights that a plaintiff himself had acquired by a breach which took the form of prolonged deceit!<sup>56</sup>

The relationship between restitutionary damages and punitive, or exemplary in the English terminology, damages, which is bound to be difficult as both purport to be "exceptional," but in different ways, has been, *mirabile dictu*, made even more tangled by a Court of Appeal which was prepared in one case to sacrifice "logic" to "practical justice" in its haste to use restitutionary damages effectively to punish an admittedly odious defendant.<sup>57</sup>

In all her papers, Roberts acknowledges that the principles of the quantification of restitutionary damages remain to be properly worked out, but in that part of the law of England and Wales where liability to disgorge has taken the most firm hold, breach of negative covenant in conveyances

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55. See *Attorney Gen. v. Blake*, [2001] 1 A.C. 268 (H.L.(E.)) 268, 277, 291 ("[T]he Solicitor General . . . argued for a recognition of an action for disgorgement of profits against a contract breaker where four conditions are fulfilled."). Lord Steyn continued:

(1) There has been a breach of a negative stipulation. (2) The contract breaker has obtained the profit by doing the very thing which he promised not to do. (3) The innocent party (in this case the Crown as represented by the Attorney General) has a special interest over and above the hope of a benefit to be assessed in monetary terms. (4) Specific performance or an injunction is an ineffective or virtually ineffective remedy for the breach. The Solicitor General persuaded me that in the case of *Blake* each of these conditions is satisfied. But since I recognise that it would be wrong to create a remedy simply to cover this case, it is right that I should explain the specific considerations which lead me to conclude that it is right on a principled basis to develop the law in a way which covers this case and other cases sharing materially similar features.

*Id.* at 291.

56. See *Experience Hendrix LLC v. PPX Enterprises Inc.*, [2003] EWCA (Civ) 323 (finding that although the defendant had used recordings of Jimi Hendrix in violation of a prior settlement, "the case was not exceptional to the point that the court should award an account of profits"); *Campbell & Wylie*, *supra* note 32 (discussing *Experience Hendrix*).

57. *Borders (U.K.) Ltd. & Others v. Comm'r of Police of the Metropolis & Another*, [2005] EWCA (Civ) 197 at [28]; see also David Campbell & James Devenney, *Damages at the Borders of Legal Reasoning*, 65 CAMBRIDGE L.J. 208 (2006) (discussing *Borders*).

of land, not only is liability a dreadful mess, but the principles of quantification are nothing more than guesswork. The best that we have been told is that the hypothetical deal "has to feel right"<sup>58</sup> to the Court, and this standard (if this is the right word) is supposed to be justified because these are "matters of judgment which are incapable of strict rational and logical exposition from beginning to end."<sup>59</sup>

Finally, the feared clash between valued contract principles and the new restitutionary damages has occurred in a case in which there can be no doubt that the agreement of the parties was effectively rewritten in order to lead to an award of restitutionary damages,<sup>60</sup> something for which there is important "authority" in the canon of the Birksian argument.<sup>61</sup>

One could go on,<sup>62</sup> but this is enough and more than enough. I have discussed all the cases I have just mentioned in other work and could only

58. *Amec Dev. Ltd. v. Jury's Hotel Mgmt. (U.K.) Ltd.*, [2001] 1 E.G.L.R. 81, 87; see also David Campbell, *The Extinguishing of Contract*, 67 MOD. L. REV. 818, 821–23 (2004) (discussing *Amec*).

59. *Amec*, [2001] 1 E.G.L.R. at 87.

60. See *infra* text accompanying notes 198–201 (discussing *Lane v. O'Brien Homes*, [2004] EWHC 303 (QB)).

61. See discussion *infra* Part VIII (discussing *Wrotham Park Estate Co. v. Parkside Homes Ltd.*, [1974] 1 W.L.R. 798 (Ch.D.)).

62. The two cases I have not mentioned which seem to have the greatest possibility of effecting commercial relationships are *Eso Petroleum Co. Ltd. v. NIAD*, [2001] EWHC 6 (Ch.) and *WWF—World Wide Fund for Nature (formerly World Wildlife Fund) v. World Wrestling Fed'n Entm't Inc.*, [2007] EWCA (Civ) 286, [2008] 1 W.L.R. 445. The former arguably is the most expansive interpretation of the Birksian argument in the case law. The latter seems to be a determined attempt to halt the Birksian argument in its tracks which, should it be followed, will be a most important case. However, both of these cases are, in their different ways, particularly difficult and confused, and they so far have not had much influence on the subsequent law, nor, indeed, have been adequately discussed in the secondary literature. McGregor's discussion of WWF, *supra* note 39, at § 12-030, exploits the case's undeniably unnecessary and unfortunate complication to place a substantial question mark over the extent of the influence it will prove to have.

Though when they wrote there had been no cases directly on it, and after some earlier indications of the argument by leading figures of the Birksian argument had not been developed, the relationship between the equitable remedies and restitutionary damages has been explored in connection with the protection of business confidences, an area where the plaintiff's remedy typically has been an interim or final injunction. See Ter Kah Leng & Susannah H.S. Leong, *Contractual Protection of Business Confidence*, 2002 J. BUS. L. 513. I have argued that making restitutionary damages more widely available to effectively supplement the plaintiff's armoury in this area is quite indefensible. See David Campbell, *Hamlet Without the Prince: How Leng and Leong Use Restitution to Extinguish Equity*, 2003 J. BUS. L. 131. A recent case would appear (its immense length and unnecessary complication makes it difficult to determine its *ratio*) to have advocated what is essentially Leng and Leong's position. *Vercoe v. Rutland Fund Mgmt. Ltd.*, [2010] EWHC 424 (Ch) at [339–45].



repeat what I have said were I to discuss them here. I refer the U.S. audience to these cases and to my discussion of them, in which, I fear, that audience may see the United States' future foretold.<sup>63</sup> What I want to do here is to stress that the decided English cases since *Blake* show that the aim of putting Section 39 disgorgement on a sound, because circumscribed, footing is bound to encounter very serious difficulty, and to turn to the reasons why this is so. It is not the English courts' failings that has led to these problems, though there have been failings enough. It is that disgorgement of the type envisaged in Section 39 cannot be put on a sound footing, because the enterprise is wholly ill-conceived.

The related problems are three. First, R3RUE tells us that a major virtue of using restitution to attack opportunistic breach by means of disgorgement is that it will bring theoretical coherence by "stating a rule to generalize . . . commonly accepted outcomes";<sup>64</sup> but it cannot do so because a coherent doctrine of disgorgement cannot be founded on restitution. Second, the attack on opportunistic breach is to serve as the basis for the attack on the immoral or amoral attitude of Holmes's bad man in the way we have seen; but it cannot do so because, far from being immoral, the bad man's attitude is expressive of cooperation in contract of a type which the relational theory of contract should find particularly desirable. Third, implicit in this is a horrid truth that completely undermines the idea of regarding breach as a wrong. Breach of contract is not a wrong in any other

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63. Professor Saiman has interestingly argued that the prospects for the reception of R3RUE generally are bleak because the abstract, doctrinal nature of the Birksian argument is at odds with the legal realist tradition of U.S. adjudication in the area Birks would call obligations. See Chaim Saiman, *Restating Restitution: A Case of Contemporary Common Law Conceptualism*, 52 VILL. L. REV. 487 (2007); Chaim Saiman, *Restitution in America: Why the U.S. Refuses to Join the Global Restitution Party*, 28 OXFORD J. LEGAL STUD. 99 (2008). In my opinion, Saiman gives far too much credence to the theoretical coherence of Birks's work, and he would have done well to give more weight to Professor Hedley's devastating criticisms of that work. See generally, e.g., STEVE HEDLEY, *RESTITUTION: ITS DIVISION AND ORDERING* (2001); Steve Hedley, *The Taxonomic Approach to Restitution, in NEW PERSPECTIVES ON PROPERTY LAW, OBLIGATIONS AND RESTITUTION* 151, 151–63 (Alistair Hudson ed., 2004). But, whatever the merits of Saiman's views of the nature of Birks's theory, it is far more important that his argument surely is undermined by the decided modern restitution cases, in relationship to contract but even more so elsewhere, which make Birks's claim to be pursuing the elimination of "discretionary remedialism," see Peter Birks, *Three Kinds of Objection to Discretionary Remedialism*, 29 U.W. AUSTL. L. REV. 1 (2000), a joke at its own expense. See David Campbell, *Classification and the Crisis of the Common Law*, 26 J.L. & SOC'Y 369 (1999) (book review). On the relationship of Birksian taxonomy and legal realism from a position sympathetic to Birks, see Hanoch Dagan, *Legal Realism and the Taxonomy of Private Law, in STRUCTURE AND JUSTIFICATION IN PRIVATE LAW* ch. 8 (Charles E.F. Rickett & Ross Grantham eds., 2008).

64. RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39 cmt. a (2011).

than a technical way. Rather, it is an essential legal institution indispensable to the efficient functioning of market economies. To the extent that restitutionary damages are set against the wrong of breach, they will not be chosen by parties who value that institution and who contract on the basis of the Holmesian choice. Such damages cannot be made of wide application whilst there is freedom of contract, for parties with freedom of choice would normally oust the restitutionary position if it was made the default basis of remedies.

#### *IV. Restitution Cannot Ground Disgorgement*

In the architecture of R3RUE as set out in its overall table of contents, breach of contract is not included in Chapter 5 on "restitution for wrongs," which is confined to two categories, "benefits acquired by tort or other breach of duty" and "diversion of property rights at death."<sup>65</sup> But this exclusion, as R3RUE makes clear, is merely a consequence of a decision to keep the relevant sections on contract within one chapter,<sup>66</sup> and Section 39, which addresses "an instance of restitution for benefits wrongfully obtained . . . is identical in principle to the claims described in Chapter 5,"<sup>67</sup> turns on the belief that the breaches it addresses are "a wrong." It was essential that R3RUE follow one of Birks's fundamental conceptual arguments in regarding breach as a wrong, for it is only by doing so that an innovation such as Section 39 is made possible. I will set out the argument derived from Birks briefly, and then show it to be a wholly suspect argument in relation to contract and, as such, the source of the problems we have discussed.

It is, of course, uncontroversial that restitutionary recovery may be obtained when a valuable benefit is conveyed to a party who subsequently breaches and who therefore would be unjustly enriched if he retained the benefit.<sup>68</sup> These "quasi-contractual" cases are divided in the law of England

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65. *Id.* ch. 5 topic 1; *id.* ch. 5, topic 2.

66. *See id.* § 39 cmt. a ("The rule of this Section has been placed in Chapter 4 rather than Chapter 5 in order to group together, for clarity of exposition, the divergent and contrasting themes of restitution in a contractual context.").

67. *Id.*

68. *See, however,* Kull's interesting remarks on quasi-contract in Andrew Kull, *Restitution as a Remedy for Breach of Contract*, 67 S. CAL. L. REV. 1465, 1485–90 (1994) (critiquing quasi-contract and restitution). I myself believe that the law is uncontroversial only in the sense that it is currently settled, for I am of the opinion that the law of contractual remedies in general would be much improved by the abolition of the quasi-contractual

and Wales into those in which the valuable benefit is a payment of money, such as a payment in advance for goods not delivered, for which the remedy is an action for monies had and received, and those in which the benefit is a performance other than a payment of money, such as construction work for which payment is not made, for which the remedy is a *quantum meruit*. This distinction is treated as a mere practical difference of quantification in the U.S. law of contract,<sup>69</sup> and, indeed, both actions do rest on a common jurisprudential basis. Both are cases of what Birks called "restitution of subtraction," because the valuable benefit is subtracted from the plaintiff, to which must be contrasted "restitution for wrongs,"<sup>70</sup> which will be set out shortly.<sup>71</sup> For the moment, we must note that it is very important to realize that the paradigm case of opportunistic breach, the efficient breach, is not a case of subtraction.

Many criticisms of the concept of efficient breach are not, in fact, direct criticisms of that concept at all. They are criticisms of a breach that leaves the plaintiff inadequately compensated because of the practicalities of obtaining an adequate remedy. This is the specific problem contemplated in R3RUE.<sup>72</sup> This can be pursued, as it is pursued by

remedies and am preparing a statement of this argument.

69. See RESTATEMENT (SECOND) OF CONTRACTS § 371 cmt. a (1981) ("If the benefit consists simply of a sum of money received by the party from whom restitution is sought, there is no difficulty in determining this amount. If the benefit consists of . . . services or property, its measurement in terms of money may pose serious problems.").

70. BIRKS, *supra* note 3, at 22–25. It is possible to trace the thinking back to Birks's noted 1982 *Current Legal Problems* lecture. Peter Birks, *Restitution and Wrongs*, 35 CURRENT LEGAL PROBS. 53 (1982). The concept of subtraction has, of course, been identified in the U.S. scholarly literature. See, e.g., E. ALLAN FARNSWORTH, CONTRACTS Vol. III p. 329 (4th ed. 2004) ("Restitution as a remedy for breach of contract is limited to benefits that are regarded as having somehow flowed from the injured party, a party that can be said to have 'lost' something that the party in breach is being asked to 'restore.'"); see also E. Allan Farnsworth, *Your Loss or My Gain? The Dilemma of the Disgorgement Principle in Breach of Contract*, 94 YALE L.J. 1339, 1370–82 (1985).

Though he ultimately identifies "unjust enrichment" as what is really at issue, it is not, in fact, possible to trace the development of the crucial distinction between "restitution of subtraction" and "restitution for wrongs" through Kull's own work, for, on the basis of his understanding of restitution of subtraction as "restoration," see Andrew Kull, *Rationalising Restitution*, 83 CAL. L. REV. 1191, 1212–15, 1219–22 (1995); see Kull, *supra* note 16, at 2031–38, he takes the novel line of trying to develop a general law of rescission. See Kull, *supra* note 68, at 1491–99; Andrew Kull, *Rescission and Restitution*, 61 BUS. LAW. 569 (2006). I believe this is highly interesting, and, for what it is worth, in my opinion it is the way the law should be developed in this area. But it does not map on to the law of restitution, in the Birksian argument or in general, at all easily.

71. See *infra* text accompanying notes 76–77 (discussing restitution for wrongs).

72. RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39 cmt. h (2011)

Roberts,<sup>73</sup> into the way the mitigation rules so reduce the defendant's liability that the rewards of successful suit are too small to justify to the plaintiff the expense and risk of (the threat of) litigation. As Stewart Macaulay put it in an important paper:

Limit[ing] remedies allows stronger parties to walk away from burdensome obligations at low or no cost. Courts frequently find that a stronger [party] has breached a contract, but so limit the remedy awarded the weaker that the victory is hollow.<sup>74</sup>

These are powerful criticisms of the operation of the law of remedies which must be taken onboard. Much of what we can hope usefully to say about particularly consumer law must turn on them. But they are criticisms of the shortcomings of civil procedure and of the operation (and design) of contract rules in the light of those shortcomings. They are not criticisms of the concept of efficient breach.<sup>75</sup> Analytically, in efficient breach, the

("In a market context, gain to one party is normally offset or exceeded by loss to the other; while the test of efficiency will not be met unless the injured party is fully indemnified against the cost of resolving the resulting dispute.").

73. See Roberts, *Restitutionary Disgorgement*, *supra* note 12, at 171–75 ("[T]he primary thrust behind the mitigation principle is don't be lazy—instead avoid unnecessary consequences. It asks the nonbreaching party to participate and avoid consequences by stopping or by acting. Mitigation's focus on the nonbreacher runs counter to disgorgement principles.").

74. Stewart Macaulay, *An Empirical View of Contract*, 1985 WIS. L. REV. 465, 470; see also *id.* at 469–70 (citing the rule in *Hadley v. Baxendale*, "[Courts] limit the remedy to the difference in value between the contract as performed and as it should have been had there been no breach. While this sounds reasonable, the burden of proof usually confines diminution in value to a token remedy" (citations omitted)); Ian R. Macneil, *Essays on the Nature of Contract*, 10 N.C. CENT. L.J. 159, 183–84 (1980) (discussing several issues with procuring full recovery including: limited recoveries due to foreseeability or certainty, litigation costs, risks inherent in litigation and the difficulty of enforcing judgments); Ian R. Macneil, *Efficient Breach of Contract: Circles in the Sky*, 68 VA. L. REV. 947, 947–60 (1982) (discussing the effect of transaction costs on breach). See generally Ian R. Macneil, *Contract Remedies: A Need for a Better Efficiency Analysis*, 144 J. INSTITUTIONAL & THEORETICAL ECON. 6 (1988).

75. From his earlier work, it is not clear whether Kull ever allows of efficient breach proper, for he seems to identify efficient breach with "a conscious decision to give the plaintiff less than what was promised." Kull, *supra* note 16, at 2051. It certainly is the case that his position is far stronger when the breach is not, in fact, efficient.

In what seems to be the most influential criticism of efficient breach from a conventional perspective, Professor Friedmann tells us that Posner's treatment of efficient breach rests on "the implied assumption [that it] entails no transaction costs. This is, however, totally unrealistic." Daniel Friedmann, *The Efficient Breach Fallacy*, 18 J. LEGAL STUD. 1, 6–7 (1989). I do not think this entirely fair to Posner, certainly not to his later statements of efficient breach, see *supra* note 28, but, however this is, it does not tell against the concept of efficient breach. The same point could be made against *all* breaches, or, to

plaintiff is adequately compensated. It is efficient only because of this. As this is so, then, again analytically, there is no subtraction in efficient breach cases, because the plaintiff *is* compensated. There can be no restitution in efficient breach cases on the same ground that it is settled that there may be restitution in quasi-contractual cases.

In light of this, the necessity of "restitution for wrongs" for the development of a law of restitution of wider application to contract situations becomes clear.<sup>76</sup> Restitution of subtraction is but an indirect and poor way of driving at unjust enrichment, and enrichment "by doing wrong to"<sup>77</sup> is a much closer approximation to the real target. Though Birks did not, to my knowledge, directly address the principal law and economics literature on efficient breach, which I have no doubt he would have regarded as completely misdirected, the concept of restitution for wrongs is intended, *inter alia*, to embrace the situation described as efficient breach, and it readily can do so. If breach is objected to as a wrong, from which the defendant should not be allowed to profit, then restitution for wrongs, as an apparently more direct attack on such profit, can do more to discourage or prevent breach than expectation-based remedies, which are directed at the compensation of the defendant, and so only indirectly, if at all, at the defendant's profit. The drive behind both of the leading English cases, *Wrotham Park* and *Blake*, and most of the intervening cases, was that the plaintiff would have received only nominal damages in these cases if confined to an expectation-based measure. Grounding restitution in the plaintiff's profits—in part in *Wrotham Park*, and in full in *Blake*—was a

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put the argument the other way around, any "transaction costs" of an efficient breach can be compensated as incidental damages to just the extent as they would be in regard of other breaches, and, more than this, the concept of efficient breach absolutely requires that they will be compensated in this way. There can be no doubt Friedmann wants to attack the very concept of efficient breach: "[S]uch a taking of an entitlement, for the sake of private gain, runs counter to the very basis of private law." *Id.* at 23. But his principal arguments are not directed at, or at least do not hit, the concept.

76. BIRKS, *supra* note 3, at 313–57. The basic theoretical development of this category was more couched in terms of tort, and, indeed, it might be said that an effect of treating breach of contract as a wrong is to assimilate it with tort, a point which pervades the Birksian argument), *id.* at 44, 334 ("Restitution for breach of contract is part of restitution for wrongs."); see also Peter Birks, *The Concept of a Civil Wrong*, in PHILOSOPHICAL FOUNDATIONS OF TORT LAW 29, 33 (David G. Owen ed., 1995) ("[A] failure to perform a contract or to fulfil an obligation to make restitution of unjust enrichment . . . is no less capable of being described as a breach of duty than negligent injury or defamation or any other familiar tort."), and is surely strongly implied by the architecture of R3RUE. See *supra* note 65 and accompanying text (noting the structure of R3RUE as it relates to Section 39).

77. BIRKS, *supra* note 3, at 23–24.

shift to what we might, allowing a certain rewriting of the actual pleadings to get at the concepts, call treating breach as a wrong.

This shift is the point of *Wrotham Park* and *Blake*, which involved breaches which might be described as "opportunistic" in that they were deliberate; they were profitable in that there were "gains to the defendant (net of potential liability in damages) greater than the defendant would have realized from performance of the contract";<sup>78</sup> and they resulted in inadequate protection to the promisee's contractual entitlement because, compensatory damages being nominal, a promisee's right to recover damages for a breach affords inadequate protection.<sup>79</sup> In *Wrotham Park*, the plaintiff's predecessor in title conveyed part of an estate to the defendant's predecessor in title.<sup>80</sup> The conveyance contained a restrictive covenant by which development of the land had to conform with a lay-out plan approved by the vendor or his successor in title.<sup>81</sup> The defendant, a developer, breached the covenant by building fourteen houses in excess of the plan.<sup>82</sup> It was found that "[n]o damage of a financial nature has been done to the plaintiff by the breach of the lay-out stipulation [and t]he plaintiff's use of the Wrotham Park Estate has not and will not be impeded."<sup>83</sup> This would, of course, have meant that the plaintiff's damages quantified on the normal diminution in value measure would be nominal.<sup>84</sup> As the court was reluctant to grant a mandatory injunction which would have meant the houses had to be demolished, the award of nominal damages effectively would have been a costless permission to the defendant to breach.<sup>85</sup> This was a situation in which the court felt that "justice [would] manifestly not have been done,"<sup>86</sup> and so it gave the plaintiff

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78. RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39 (2011).

79. *Id.* § 39(2)(c) (Tentative Draft No. 4, 2005).

80. *Wrotham Park Estate Co. v. Parkside Homes Ltd.*, [1974] 1 W.L.R. 798 (Ch.D.) 799.

81. *Id.*

82. *Id.* at 804.

83. *Id.* at 811.

84. *See id.* at 812 ("[T]he damages [would be] nil or purely nominal, because the value of the Wrotham Park Estate as the plaintiffs concede is not diminished by one farthing in consequence of the construction of a road and the erection of 14 houses on the allotment site.").

85. *See id.* ("If, for social and economic reasons, the court does not see fit in the exercise of its discretion, to order demolition of the 14 houses, is it just that the plaintiffs should receive no compensation . . . ? Common sense would seem to demand a negative answer to this question.").

86. *Id.* at 815.

damages representing the price the defendant would have had to pay to obtain a release from the covenant, which the court estimated at 5% of the profit the defendant made from the breach.<sup>87</sup>

*Wrotham Park* was not decided as a restitution case. The court believed itself to be exercising a power to award damages which is based in nineteenth century equity jurisprudence, and the first theoretical rationalization made of the award in modern terms was of it as "hypothetical release" or "lost opportunity to bargain" damages,<sup>88</sup> which are a form of compensatory damages, albeit quite different from (and contradictory of) compensatory damages as we normally understand them. But, following considerable turmoil in a succession of cases,<sup>89</sup> in *Blake*, the House of Lords identified *Wrotham Park* as one of the "appropriate situations" in which a "restitutionary claim for the profits made from a breach of contract" should be recognized.<sup>90</sup> The Lords saw the importance of *Wrotham Park* to be that it offered the possibility of correcting a situation in which contracts "may be breached with impunity," which would be "a sorry reflection on the law."<sup>91</sup> As the plaintiff got only part of the defendant's profits, *Wrotham Park* was a case of what has since been called "partial" restitution or disgorgement. *Blake* itself was a "total" restitution or disgorgement case.

In *Blake*, the restitutionary remedy was used to attempt to prevent a profit arising from conduct which was an egregious moral wrong. Between 1944 and 1960, George Blake was employed by the British security services.<sup>92</sup> As a condition of his employment he signed a declaration of compliance with the Official Secrets Act,<sup>93</sup> and in the proceedings in *Blake* this was held to be a simple contractual undertaking not to divulge official

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87. *Id.* at 816. There is some obscurity about the measure of profit, though much less than in most other cases, and it does not affect the argument.

88. Robert J. Sharpe & S.M. Waddams, *Damages for Lost Opportunity to Bargain*, 2 OXFORD J. LEGAL STUD. 290 (1982); *infra* note 191 and accompanying text.

89. See HARRIS ET AL., *supra* note 32, ch. 17 (discussing the leading cases); Campbell & Harris, *supra* note 32 (same). The leading cases are *Bracewell v. Appleby*, [1975] Ch. 408, *Surrey C.C. v. Bredero Homes Ltd.*, [1992] 3 All ER 303 (Ch.D.), [1993] 1 W.L.R. 1361 (C.A.), and *Jaggard v. Sawyer*, [1995] 1 W.L.R. 269.

90. *Attorney General v. Blake*, [2001] 1 A.C. 268 (H.L.(E.)) 282–83.

91. *Id.* at 283.

92. *Id.* at 275.

93. See Official Secrets Act, 1989, c. 6, § 1 (Eng.) ("[A] person . . . is guilty of an offence if without lawful authority he discloses any information, document or other article relating to security or intelligence which is or has been in his possession by virtue of his position as a member of any of those services . . .").

information.<sup>94</sup> In 1961, Blake was imprisoned in England for espionage.<sup>95</sup> However, in 1966 he escaped from custody, and he has since lived in the foreign country for which he was a spy.<sup>96</sup> In 1989 he agreed with a U.K. publisher to publish an autobiography for which he was to receive an advance of £150,000.<sup>97</sup> As in *Wrotham Park*, compensatory damages for this breach would have been nominal, but the then Attorney General, no doubt mindful of a predecessor's previous humiliating failure to prevent publication of Peter Wright's *Spycatcher* disclosures about the secret services,<sup>98</sup> largely because foreign publication made granting a domestic injunction ridiculous,<sup>99</sup> wisely did not seek an injunction to prevent publication, but he did seek to prevent Blake from receiving the £90,000 that remained to be paid of his advance (£60,000 had been paid and obviously was practically irrecoverable).<sup>100</sup> The manifest unsavouriness of allowing conduct like Blake's eventually to yield a benefit to him<sup>101</sup> led their Lordships<sup>102</sup> to generalize a restitutionary remedy which would completely cover Blake's breach of his simple contractual undertaking not to divulge official information by enforcing recovery of his advance from his publisher.

The total restitution or disgorgement in *Blake* has been run together with partial restitution or disgorgement in *Wrotham Park* to create what has since been called a "sliding scale" of restitutionary or disgorgement damages. The sliding scale certainly was implicit particularly in Lord Nicholl's leading speech in *Blake*,<sup>103</sup> and has been made explicit in an account of his extra-judicial views:

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94. See discussion *infra* Part X.

95. *Blake*, [2001] 1 A.C. at 268.

96. See *id.* ("In 1966 Blake escaped from Wormwood Scrubs prison and fled to Berlin and then to Moscow. He is still there, a fugitive from justice.")

97. *Id.*

98. See generally Attorney Gen. v. Observer Ltd., [1990] 1 A.C. 109.

99. See MALCOLM TURNBULL, THE SPYCATCHER TRIAL 299 (1989) ("[The Judge] held that henceforth, given the wide circulation of *Spycatcher* throughout the rest of the world, newspapers were free to report its contents in the United Kingdom.")

100. Attorney General v. Blake, [2001] 1 A.C. 268 (H.L.(E.)) 275.

101. See *infra* notes 240–46 and accompanying text (discussing the atmosphere surrounding the *Blake* case).

102. Following a strategy advocated by Birks: Peter Birks, *Restitutionary Damages for Breach of Contract: Snapp and the Fusion of Law and Equity*, 1987 LLOYD'S MARITIME & COM. L.Q. 421.

103. See HARRIS ET AL., *supra* note 32, at 261–62 ("In *Blake*, Lord Nicholls explicitly stated that, to the extent *Wrotham Park* and *Bredero Homes* are inconsistent, the former is to be preferred.")



Once one had crossed the threshold for being able to recover an account of profits for breach of contract, rather than compensatory damages or specific relief, Lord Nicholls thought that the measure of recovery could extend from expense saved through to stripping a proportion of the profits made through to stripping all the profits made from the breach. The *Wrotham Park Estate* case (where 5 per cent of the profits had been stripped) was therefore based on the same principles as *A.-G. v Blake* (where all the profits had been stripped).<sup>104</sup>

There are immense and, in my opinion, irresolvable problems with the entire argument for a unified category of restitutionary damages which have given rise to the unsatisfactory English cases mentioned above.<sup>105</sup> I wish to focus here on the fundamental problem, which generates the others. This is that, in seemingly completing itself in *Blake*, the Birksian argument for the wider availability of restitution for breach of contract actually annihilated itself.<sup>106</sup> Obviously, restitution of subtraction can be subsumed under restitution for wrongs, for the breach that yields an unjust enrichment is a wrong whether or not there is subtraction. What is more, the point can be turned around, for if wrongful breach is abhorrent in cases of subtraction, it also is abhorrent in cases without subtraction, for the wrong of breach is present in both. This is precisely why restitution for wrongs seemed to be necessary to deal with *Wrotham Park* and *Blake* situations in which compensatory damages would have been nominal, for there was no loss to compensate, and therefore no subtraction. Especially after it had been subjected to such devastating exposure of its rococo over-elaboration as that mounted by Hedley,<sup>107</sup> one can forget that Birks's basic idea was very simple. It was to make "restitution" embrace not merely "giving back," but also "giving up."<sup>108</sup> Birks used to insist that the underlying Latin "restituere/restitution" could embrace both of these situations,<sup>109</sup> which map on to restitution of subtraction and restitution for wrongdoing. The former

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104. Andrew Burrows & Edwin Peel, *Breach of Contract, Restitution for Wrongs, and Punishment: Review of Discussion*, in COMMERCIAL REMEDIES, *supra* note 46, at 129.

105. See discussion *supra* Part III (discussing the English cases).

106. Birks's criticisms of the incoherence of quasi-contract, BIRKS, *supra* note 3, at 29–39 ("[T]he whole law of quasi-contract belongs inside the law of restitution."), largely survive the failure of his proposed alternative.

107. See Hedley, *Taxonomic*, *supra* note 63, at 162 ("[T]he supposedly solid roots of restitutionary theory are in fact distinctly shaky. What is presented as clear in principle actually rests on no more than repeated assertion.").

108. Peter Birks, *Equity and the Modern Law*, 26 U.W. AUSTL. L. REV. 1, 28 n.57 (1996).

109. *Id.*

certainly was grounded in authority, and the latter was intended to be able to borrow on this quality to sanction its attempt to extend restitution to cover giving up situations.

But the very idea of restitution in the concept of restitution for wrongdoing is extremely problematic. As there is no subtraction, there is no valuable benefit conveyed, and therefore there is nothing to be restored. The edifice collapses. There can be no *restitution* of wrongs as a category potentially covering all breaches, for cases other than cases of subtraction, the very cases that were to be handled better as a result of the innovation, cannot be restitution cases. All this seemed to dawn on Birks as the cases decided purportedly in line with his thinking threw up serious problems with restitution itself, and he was engaged on two fresh starts bringing "unjust enrichment" rather than "restitution" to the fore at the time of his death.<sup>110</sup> I would advise the U.S. audience concerned with the relationship of restitution and contract simply to ignore these. (Of course, that audience is at perfect liberty to disregard my advice.)<sup>111</sup> In my opinion, which authoritative figures do not share, they both are markedly poor, especially by comparison to the brilliance of *An Introduction to the Law of Restitution*,<sup>112</sup> and add only confusion to the study of that relationship.<sup>113</sup>

The broad thrust of Birks's later work is to adopt a "multi-causal" approach which, I will merely assert here in respect of Birks himself, gives up the attractive unifying thrust of his early work. Not all of Birks's reasons for wanting to abandon restitution and speak of unjust enrichment, framed across the whole of the law of obligations, are relevant to us. But

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110. See PETER BIRKS, *UNJUST ENRICHMENT* 4 (2d ed. 2005) ("The law of gain-based recovery is larger than the law of unjust enrichment. Every unjust enrichment gives rise to a right to restitution, but that proposition cannot be turned round . . . Restitution is not mono-causal."); Peter Birks, *Misonmer*, in *RESTITUTION: PAST, PRESENT AND FUTURE* ch. 1 (W. Cornish et al. eds., 1998) ("[W]e ought to call our subject unjust enrichment."). Despite talking in the most radical tones of the need to break with his earlier work, I think Birks sometimes inconsistently maintained his aim to "extend" the meaning of restitution in his later work. E.g., Birks, *Unjust Enrichment and Wrongful Enrichment*, *supra* note 4, at 1773, 1781 ("[T]he law of restitution was to be the law of rights to a giving up: a person with a restitutionary right was a person with a right that another give up something, no matter whether the giving up was or was not a giving back.").

111. The U.S. readership of this Article may most conveniently begin to make its mind up by looking at Birks, *A Letter to America: The New Restatement of Restitution*, *supra* note 4.

112. BIRKS, *supra* note 3.

113. It seems significant that Birks got into such a quandary over what he was doing that he did not even really settle on unjust enrichment, but at one point was prepared to use a terminology of "disgorgement" if that terminology could be "universally adopted": Birks, *Misonmer*, *supra* note 110, at 12–13.

with respect to breach of contract, this shift seems pointless, for an enrichment "rule" does not allow us "to generalize . . . commonly accepted outcomes"<sup>114</sup> any more than did a restitution "rule." If breach is wrongful, why should the empirical incident that the defendant is enriched by it matter? Let us imagine that a defendant breaches in order to make a profit by moving to a new contract, but fails to do so because of unforeseen problems with the new contract. Is it defensible that he should make no "restitution" of his "unjust enrichment?" Can a distinction be drawn between such a case and an otherwise identical breach from the point of view of the plaintiff in which the defendant is enriched because he does make the expected profit?

The main response to all this in the Commonwealth literature<sup>115</sup> has been to, in effect, go back to the distinction between restitution of subtraction and restitution for wrongs, which reappear as, in the terms of Dr. James Edelman (as he then was),<sup>116</sup> "restitution" and "disgorgement." Edelman's version of the "multi-causal" argument, benefitting from early endorsement by Birks,<sup>117</sup> has attracted the most discussion, including by Roberts,<sup>118</sup> who regards it highly. It is, I think, instructive to say something about Edelman's views,<sup>119</sup> for they show where the U.S. argument must, I think, go, and where, indeed, Roberts has already gone.

114. RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39 cmt. a (2011).

115. I ignore the development of the philosophy of "restitution" and "unjust enrichment" which, despite recent distinguished contributions by e.g. Professor Dagan, still is principally associated with Professor Weinrib. In briefest compass, the point I am trying to make here would cut against Weinrib's basic argument that "the principle of unjust enrichment [is] an embodiment of corrective justice," see Ernest Weinrib, *The Normative Structure of Unjust Enrichment*, in STRUCTURE AND JUSTIFICATION IN PRIVATE LAW, *supra* note 63, at 43, because corrective justice means two quite different things in subtraction and nonsubtraction contract cases, or, to put the point more strongly in the way I would prefer, there is no injustice to correct in nonsubtraction contract cases. The point is impossible to make at reasonable length in the context of a criticism of the Birksian argument because Weinrib has always had a far more sophisticated view of breach of contract than Birks.

116. Edelman has recently been appointed to the Supreme Court of Western Australia.

117. See Birks, *Unjust Enrichment and Wrongful Enrichment*, *supra* note 4, at 1773–74 ("Edelman calls the former a restitutionary award for the wrong, the latter a disgorgement award or, more straightforwardly, 'restitutionary damages' and 'disgorgement damages.' His work . . . argues strongly for the legitimacy of gain-based awards, and it succeeds in showing that there are two quite different measures." (citations omitted)).

118. See generally Roberts, *Commonwealth of Perspective*, *supra* note 12, at 954–61.

119. I will not, however, go into the case law in which Edelman's argument has been discussed, which would not, in my opinion, justify the length of treatment necessary to explain much of this typically not very penetrating judicial *dicta* to a U.S. audience: e.g. WWF—World Wide Fund for Nature (formerly World Wildlife Fund) v. World Wrestling Fed'n Entm't Inc., [2007] EWCA (Civ) 286, [2008] 1 W.L.R. 445.

For Edelman, "restitution" and "disgorgement" are two forms of "gain-based damages."<sup>120</sup> As I have argued elsewhere,<sup>121</sup> this is in itself unobjectionable, but only because it is wholly reactionary.<sup>122</sup> Having two forms of damages avoids the problems of Birks's attempt to unify the field in terms of restitution, but only by returning to the position prior to the attempt, as Edelman's category of gain-based damages has no theoretical integrity in itself. In Edelman, restitution is confined to its acknowledged bounds prior to Birks, to giving back in situations of subtraction, and disgorgement is confined to giving up in other situations, which were also recognized prior to Birks. In a number of situations broadly related to contract, disgorgement has, of course, long been available. In *Blake*, a "light sprinkling of cases where courts have made orders having the same effect as an order for an account of profits"<sup>123</sup> are used as the springboard authority for *Blake*'s extension of the restitutionary or disgorgement remedy to breaches of simple contract. The clearest one is breach of the many fiduciary duties, which Edelman stresses. We are on relatively solid ground here, and, speaking generally, one can say that good arguments have been made for disgorgement in some specific circumstances. But why is gain-based damages identifiable as a theoretical category, other than by its merely empirical effect? Edelman subsumes restitution and disgorgement under the rubric of gain-based damages,<sup>124</sup> but, with respect, this is perfectly straightforward. What is not straightforward, and what Edelman does not do, is theoretically unify them. What was restitution or unjust enrichment in Birks is now gain-based damages in Edelman, but, though the name changes, the problem remains the same. Or, indeed, the problem gets worse, as one can concede the abstract attractiveness of Birks's attempt to bring taxonomical neatness to the law of obligations, but Edelman's taxonomy begins by giving this up, and there is nothing put in its place.

Edelman's general reason for awarding gain-based damages is that the plaintiff has a "legitimate reason" for seeking them,<sup>125</sup> but this reason, derived from *Blake* and the more or less settled case law prior to it, is a

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120. JAMES EDELMAN, GAIN-BASED DAMAGES 65 (2002). For a recent statement by Edelman of the multi-causal approach, see generally James Edelman, *The Measure of Restitution and the Future of Restitutionary Damages*, 18 RESTITUTION L. REV. 1 (2010).

121. See Campbell, *supra* note 13 (noting that the combination of restitution and disgorgement is unobjectionable).

122. See generally EDELMAN, *supra* note 120, at 36–41.

123. Attorney Gen. v. Blake, [2001] 1 A.C. 268 (H.L.(E.)) 284.

124. *Supra* note 120 and accompanying text.

125. EDELMAN, *supra* note 120, at 189.

truism (as it was in *Blake* and the previous law) which adds nothing to the discussion, and the concrete reasons Edelman gives for awarding restitution or disgorgement are very much the ones (including the legitimate reason) for which they would have been awarded in the law prior to *Wrotham Park* and *Blake*. But, leaving restitution in Edelman's sense aside because this unarguably covers subtraction cases, Edelman wants disgorgement to be extended to breach of simple contract just as much as Birks, and to the fiduciary duty and other existing occasions for disgorgement, he adds a new one of general scope: in essence, cynical breach when compensatory damages will leave the defendant with a profit. But, as I have said,<sup>126</sup> that this is quite untenable began to emerge somewhere between the Court of Appeal's and the House of Lords's judgments in *Blake* itself, and this has been emphasised in the subsequent cases.

Once one sees this, one has to ask why we should allow the extension of disgorgement sought by Edelman, and recognize there is no good answer. Edelman confesses that "it is very difficult to tell when the law will consider that a plaintiff has a legitimate interest,"<sup>127</sup> and he cannot do better than this by looking to a unifying theory of restitution because he began by giving this up, not realizing that he thereby sawed away the branch on which he sat. In Birks, for good or ill depending on how far one thinks abstract classification should be driven in the common law, the apparent logic of the promised unified classification drove the extension of the restitutionary remedy to giving up situations. What drives the similar extension in Edelman? With all respect, the last thing it can be said to be is the theoretical integrity of gain-based damages, for this is, I repeat, a purely empirical category.

In my opinion, which I shall state baldly, the driving impetus behind Edelman's work, and the general attitude it expresses, is simply a thoroughgoing dislike of breach, which is largely due to a failure to understand its economic function or its legal form. Breach is seen as a "civil wrong" by a "wrongdoer" which should normally be "prevented." Compensatory damages very often do not do this, and so restitutionary and disgorgement damages should be more widely available, with *Blake* being welcomed because it makes them so.<sup>128</sup> This is merely a simple view of *pacta sunt servanda* put in fresh terms, if not in fresh thought. If one thinks

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126. See *infra* note 55 and accompanying text (noting that *Blake* itself retreated from this argument).

127. EDELMAN, *supra* note 120, at 189.

128. *Id.* ch. 5.

the law of remedies for breach of contract should recognize "powerful arguments for treating breach of contract in the same way as other wrongs"<sup>129</sup> and therefore try to prevent those breaches, then that law is inexplicable except as markedly incompetent, and Edelman's discussion of breach of contract continuously exudes puzzlement over just this. This puzzlement is what is left if one wants to prevent breach, but is sufficiently learned in the law to know that the existing law of breach of contract does not normally seek actually to prevent breach,<sup>130</sup> and is also sufficiently scrupulous not to just attempt to ride roughshod over the "obstacles" posed by the existing law.<sup>131</sup>

If one gives up Birks's classificatory scheme, then, unless one comes up with another theoretical scheme, one is left without a justification for *Blake*. It is for this reason that Friedmann's conception of a performance interest which is to replace expectation as the theoretical foundation of remedies, though it does not sit easily with a basically restitutionary law but rather really rests on conflating contractual and proprietary obligations,<sup>132</sup>

129. *Id.* at 149.

130. The most graphic display of this puzzlement in the at-all-recent Commonwealth literature is Charlie Webb, *Performance and Compensation: An Analysis of Contract Damages and Contractual Obligation*, 26 OXFORD J. LEGAL STUD. 41 (2006), which concludes with the following in the apparent belief that there is a shred of novelty to it:

If we wish to continue the current prioritization of compensatory claims, an explanation is needed as to why the claimant is barred from enforcing his right to performance. It would be more honest to admit that, in such cases, the claimant acquired no such right upon contract formation. This would have far-reaching consequences for our understanding of contract law and contractual obligation.

*Id.* at 71.

131. Edelman's discussion of exemplary damages clearly hearkens for the extension of those damages towards a wider class of breaches. See James Edelman, *Exemplary Damages for Breach of Contract*, 117 LAW Q. REV. 539 (2001) (discussing a Canadian case where exemplary damages were awarded in a breach of contract case). However, in what we can see is a characteristic style of argument, he does not just go the whole hog but tries to identify, and then extend, a category of "extreme" breaches to which exemplary damages are appropriate. *Id.* at 545. Now, this has the positive effect of making Edelman's discussion a model of restraint by comparison to a number of others, but it does leave the tricky problem of identifying the extreme cases, and, in my opinion, neither Edelman nor the case law around *Farley v. Skinner (No. 2)*, [2002] 2 A.C. 732, makes any more progress towards solving this problem than he or the case law around *Blake* has made towards solving the problem of identifying the legitimate interest.

132. See Daniel Friedmann, *Restitution of Benefits Obtained Through Appropriation of Property or the Commission of a Wrong*, 80 COLUM. L. REV. 504, 513 (1980) ("Contract relations may also give rise to interests that come within the ambit of 'property' for purposes of restitution."). Friedman continues:

The property approach is, however, relevant in situations where one person, in

has been so often welcomed by the proponents of restitution. I will say more about the performance interest in the next Part of this Article, but let us put it to one side for the moment and recapitulate on the nature of the existing law.

There are, of course, justifications given in the English law for the "light sprinkling of cases" so important in *Blake*, and there are parallel doctrines in the Commonwealth and U.S. law. However, all of these turn on the breach having a more than simple contractual element, and it is this extra element which provides the legitimate interest in seeking more than compensatory damages. To repeat Edelman and myself, breach of fiduciary duty is the clearest example. But there is no justification in existing authority for what is done in *Blake*, which, as I have noted the Court of Appeal has told us, "marks a new start in this area."<sup>133</sup> The actual justification for *Blake*, which, ultimately feeble as it is in my opinion, has worked to a surprising degree, is Birks's drive towards a unified classification of wrongs which, in respect of contract, draws on the general dislike of breach which follows from the common failure to understand its function and form. This failure (amongst other things) has caused Birks's classification to fall apart. By now giving up those parts of the classification which are most problematic, Edelman may avoid their problems,<sup>134</sup> but he also gives up the initial attractiveness of Birks's drive towards theoretical coherence.

All this convoluted theorizing tells us that there is nothing in the concept of restitution that can coherently ground liability in efficient breach

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breach of a contract, acquires a benefit not through the other party's performance but by the use of his own labor or property, or by saving the expenses that performance would require. The question of restitution arises when such a person could not have derived this benefit but for his breach of the contract.

*Id.*

133. *Experience Hendrix LLC v. PPX Enter. Inc.*, [2003] EWCA (Civ) 323, [16].

134. It is, in my opinion, better to say he merely defers consideration of the problems, for, of course, one can do without the sliding scale, but if one nevertheless wants restitutionary (hypothetical release or partial disgorgement after *Wrotham Park*) damages and disgorgement (account of profits or total disgorgement after *Blake*) damages, one still has to say when each are available, and Edelman does not manage to do this. This all emerges from Professor Burrows's criticisms of Edelman, made with the sliding scale in mind. See BURROWS, *supra* note 46, at 461–62 ("Edelman's thesis is particularly hard to reconcile with the law on restitution for breach of contract. No distinction was drawn by the House of Lords between 'disgorgement damages' and 'restitutionary damages' and, contrary to Edelman's thesis, there was no indication that . . . less restrictive criteria should apply [to the latter].").

cases. And, indeed, what lies behind the theorizing, behind *Wrotham Park* and *Blake*, and behind Section 39, is not the concept of restitution but the concept of a wrong. Perhaps "concept" is itself the wrong word, if I might put it this way. We really are dealing with something much more visceral than a concept. We are dealing with the feeling that breach is wrong. And the problem with the criticism of efficient breach in general, and Section 39 in particular, is that it is actually this feeling that is utterly wrong. To see why, we must find out the reason why contracts are breached.

V. *The Bad Man's Attitude Is Cooperative and Breach Is Not a Wrong*<sup>135</sup>

The negative attitude to efficient breach taken by R3RUE and by Roberts is also taken across the range of contractual scholarship, including by many of the leading proponents of the relational theory. Nevertheless, it is, in my opinion, mistaken. The mistake involves unduly concentrating on the Posnerian concept of efficient breach, rather than on the efficiency of breach itself. For the very considerable attention which the Posnerian concept has received is in marked contrast to the other form of "efficient breach," though this form is far more important; indeed determining the correct policy towards it is the most important issue in the law of contractual remedies. The purpose of what has been called efficient breach is to allow the defendant to maximize a gain. Macneil and others, including Kull, doubt this type of breach takes place frequently; interesting empirical research gives evidence that the notion of Posnerian efficient breach does not sit well with the business community;<sup>136</sup> and it would seem clear that that notion plays only a very minor role in deciding cases.<sup>137</sup> However this

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135. The following section draws on arguments made in David Campbell, *Breach and Penalty as Contractual Norm and Contractual Anomie*, 2001 WIS. L. REV. 681 and David Campbell, *The Relational Constitution of Remedy: Co-operation as the Implicit Second Principle of Remedies for Breach of Contract*, 11 TEX. WESLEYAN L. REV. 455 (2005). A number of the central points I attempted to make in these papers have been independently made in contributions to a symposium initially published in the *Michigan Law Review* and revised in *FAULT IN AMERICAN LAW* (Omri Ben-Shahar & Ariel Porat eds., 2010). I have not attempted to make the detailed revisions necessary to make adequate reference to this symposium in this section of this Article.

136. See David Baumer & Patricia Marshall, *Willful Breach of Contract for the Sale of Goods: Can the Bane of Business Be an Economic Bonanza?*, 65 TEMP. L. REV. 159, 171 (1992) ("[S]urvey respondents overwhelmingly rejected the notion that it is ethical for a trading partner to breach a contract deliberately because a better deal can be had elsewhere. Respondents also indicated that the wilful nature of a breach would . . . substantially increase the probability of litigation.").

137. See Craig S. Warkol, Note, *Resolving the Paradox Between Legal Theory and*



is, it is essential to see that, far more important than this maximizing breach, is the breach which has the purpose of minimizing loss.<sup>138</sup> This is, indeed, the typical case of breach, though not generally recognized as such.

When the defendant undertakes a primary contractual obligation, he does so in the belief that performance of that obligation will cost a certain amount. That this belief inevitably will be based on bounded rationality at the time of the agreement means that a risk always attends a contractual undertaking.<sup>139</sup> One risk is the Posnerian efficient-breach risk that, even if the original contract goes as planned, a better contract could have been made. In other cases, however, the risk that the original contract does not go as planned becomes manifested in a rise of the costs the defendant incurs in performing. Any rise in the cost of complete performance above the defendant's original estimate will reduce the defendant's expected profit margin, and thus the defendant's own expectation interest, and beyond a certain point the rise will extinguish that margin completely (leaving the defendant in a "break-even" contract, where receipts equal costs), or make the margin negative (leaving the defendant in a "losing contract," where receipts are lower than costs). The enormous variation in the empirical circumstances which give rise to these outcomes—unanticipated shortage of raw materials, destruction of premises by fire, etc.—should not obscure the fact that (the terms not being in dispute) it is always a rise (or an anticipated rise) in the cost of performance that gives the good faith defendant an incentive to breach.<sup>140</sup>

The allocation of risks to the parties takes place within certain limits to the extent to which any defendant can be required to absorb risk. There is a fundamental limit to the extent to which the defendant could be obliged to perform even when his costs are rising which is set by the possibility of his becoming bankrupt or going into liquidation. There is a lower limit set by

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*Legal Fact: The Judicial Rejection of the Theory of Efficient Breach*, 20 CARDOZO L. REV. 321, 334 (1998) ("With a few notable exceptions, most judges do not explicitly adhere to the precepts of the theory of efficient breach in their decisions. In cases where judges could apply the theory of efficient breach to strengthen their conclusions, they often fail to do so." (citations omitted)).

138. Cf. ROBERT COOTER & THOMAS ULEN, LAW AND ECONOMICS 263–69 (5th ed. 2008) (discussing the distinction between the "fortunate" and the "unfortunate" contingency).

139. Campbell, *Relational Constitution*, *supra* note 135, at 463.

140. *Id.* at 464. In his comments on the draft of this Article, Professor Shupack has rightly raised examples that seem to be counter-evidence to this claim, but he allows they are marginal, and I will ignore them because I believe them to be readily reconcilable with it, but that it would be inappropriate to spend the necessary time on the reconciliation here.

the possibility of the contract being discharged for reasons which in the United States are treated as commercial impracticability or frustration,<sup>141</sup> though discharge on these grounds is almost otiose because it is so rarely granted. In the great majority of cases, however, a more relevant limit is set, and the general possibility of breach *created*, by the quantification of damages according to the expectation principle. When the costs of performance exceed the costs of breach, the defendant has a rational incentive to breach. Because the costs of breach are the defendant's *and* the plaintiff's lost expectation and wasted reliance, the costs of breach can be lower than the costs of performance only if damages are normally quantified on a compensatory basis and there is an incentive to mitigate so that the plaintiff is compensated only for lost net profit; or, to put it the other way around, only if literal enforcement is an exceptional remedy. That the remedies system is like this has the result that the most important sensible course of action for the plaintiff after breach normally is to take commercial cover by finding a substitute and being compensated for his net loss, if any. Exceptions to the basic position must be considered when cover is inadequate to protect the plaintiff's expectation.

If the damages system works in the sense that damages actually are adequate, the plaintiff should be indifferent whether the defendant pays damages or performs. The issue should be whether the defendant be made to perform or to pay compensatory damages when *both* protect the plaintiff's expectation; and, if the defendant decides that breach is a less costly way of doing this than performance, then the defendant should be allowed to breach. To compel the defendant to perform will protect the plaintiff's expectation, but *ex hypothesi*, damages will do this more cheaply than literal enforcement. As no benefit will be conferred by making the defendant protect the plaintiff's expectation by the more expensive method of literal enforcement, the defendant should be allowed to elect the cheaper method.

*Nor is this a matter of being unilaterally generous to the defendant.* As rational pricing requires the parties to include the cost of potential liability for breach, the plaintiff will benefit from a price lowered because mitigation lowers the cost of liability.<sup>142</sup> I will argue below that it is competition over this aspect of contracting that has made contracts which

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141. *Id.* The analogues to these pleas of excuse in the law of England, Wales, and other commonwealth jurisdictions are by no means completely congruent with the U.S. law.

142. See Richard Craswell, *Contract Remedies, Renegotiation and the Theory of Efficient Breach*, 61 S. CAL. L. REV. 629, 657 (1988) ("By definition, a cost-effective act of mitigation will reduce the seller's liability by more than the act costs the buyer . . .").

minimize liability the norm, and that this is reflected in the expectation principle being the default rule of remedies. To do otherwise than adopt what Goetz and Scott have called this "principle of joint-cost minimization"<sup>143</sup> of loss would be to impose pointless waste on the parties which they themselves normally avoid.

It is in this context that something useful might be said about Friedman's performance interest. Here is the key passage in his influential article:

The essence of contract is performance. Contracts are made in order to be performed. This is usually the one and only ground for their formation . . . . This interest in getting the promised performance . . . the performance interest . . . is the only pure contractual interest [and] is protected by specific remedies, which aim at granting the innocent party the very performance promised to him, and by substitutional remedies.<sup>144</sup>

This passage seems to be taken to be axiomatic in most of the current literature, but, in my opinion, it contains as many serious fallacies about contracts and remedies as it would be possible to cram into so small a space. Contracts are not made in order to be performed. It is promises to exchange that are made in order to be performed. The primary obligations under the contract are promises to exchange and are a matter of economics. Contracts are made in order to obtain legal security against nonperformance by generating latent secondary obligations to provide a remedy in the event of breach. Of course, when parties express their promises to exchange in the form of a contract, it is (to some extent) in the contract that the parties specify their mutual primary obligations, but those promises could be expressed in other ways, and the decision to express them in the form of a legally enforceable contract entirely rests on the attempt to obtain the security of a remedy in the event of breach. The essence of contract is, then, not performance but (breach and) remedy.

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143. Charles J. Goetz & Robert E. Scott, *The Mitigation Principle: Toward a General Theory of Contractual Obligation*, 69 VA. L. REV. 967, 972–73 (1983). Schwartz's interesting advocacy of wider use of specific performance is readily reconcilable with this stance, for it does not envisage actual literal enforcement being the result of his suggestion but believes, generally wrongly in my view, that post-breach negotiations will be improved if that suggestion is adopted. See Allan Schwartz, *The Case for Specific Performance*, 89 YALE L.J. 271 (1979). See also the valuable comment Timothy J. Muris, *The Costs of Freely Granting Specific Performance*, 1982 DUKE L.J. 1053.

144. Daniel Friedmann, *The Performance Interest in Contract Damages*, 111 LAW Q. REV. 628, 629 (1995); cf. Friedmann, *supra* note 75, at 6–7 (offering a criticism of efficient breach).

And once this is realized, then another point follows. When one wishes to understand and properly evaluate the contract remedies system, it is absolutely vital to appreciate that, in complete contradiction of the literal understanding of *pacta sunt servanda* and its modern statement in the performance interest, it does not necessarily matter to commercial parties whether the primary obligation is performed or enforced. The legal institution of contract is the general form of regulation of economic exchange, but, in a most important sense, the legal institution is not what is essential. It is the economic exchange, and particularly the surplus that the parties intend to realize through their exchange, that is essential. The actual performance of the contract is incidental to the obtaining of the surplus, indeed it is a cost of obtaining that surplus, and an understanding of contract remedies turns on seeing that expectation of surplus is what matters, not actual performance of the obligation. In a contract which is performed, expectation is protected by performance. In a contract which is breached in good faith, something has happened to make performance more costly, and though the overriding goal remains protection of the plaintiff's expectation, this should be done as cheaply as possible, and alternatives to performance should be considered. Both the law of contract's general recourse to compensatory damages rather than literal enforcement and its mitigating principles of quantification of damages can be explained only on this basis. In sum, we might say that the fundamental goal of the law of contract is to put the plaintiff in the position he would have been in had the contract been performed (that is, to protect the plaintiff's expectation), *but by the means which imposes least cost on the defendant*. As it has been put by Andersen:

[R]emedies for breach of contract . . . attempt to accommodate two competing goals: (1) securing to the injured party the benefit of [the] bargain, (2) without imposing unnecessary costs on the breaching party.<sup>145</sup>

In the law of England and Wales, the "first principle" of contract damages is stated as "the rule in *Robinson v. Harman*": "where a party sustains a loss by reason of breach of contract, he is, so far as money can do it, to be placed in the same situation, with respect to damages, as if the

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145. Eric G. Andersen, *Good Faith in the Enforcement of Contracts*, 73 IOWA L. REV. 299, 306 (1988). One might say that the first, compensation principle of damages is supplemented by a second, efficiency principle, in an instance of the common law's combination of compensation and efficiency discussed in Cooter's seminal article. Robert Cooter, *Unity in Tort, Contract and Property: The Model of Precaution*, 73 CAL. L. REV. 1 (1985).

contract had been performed."<sup>146</sup> By stressing that the aim is to put the plaintiff where he *would* have been had the contract been performed, the rule in *Robinson v. Harman* makes protection of future expectation the basis of compensatory damages. In *Robinson v. Harman* itself, a defendant who had failed to convey a lease was liable not merely for the plaintiff's wasted expenses (in modern terms, reliance loss), but also for the extra cost of leasing a similar property from a third party (in modern terms, expectation loss).<sup>147</sup> The principal significance of *Robinson v. Harman* was that it did expand the defendant's liability, which had been thought normally to extend only to reliance loss in cases of its sort, to include expectation. But this expansion was carried out in the way sympathetic to the defendant with which we are now familiar. The expectation loss was calculated as the difference in the rent of the third party's property minus the contracted rent,<sup>148</sup> i.e., in modern terms, market damages when, to labour the point, the plaintiff mitigates by securing a substitute.

I submit that the full significance of *Robinson v. Harman* lies in its articulation of *two* principles of contract damages: protection of the plaintiff's expectation, but protection in such a way as to minimize the defendant's expense. If the protection of the plaintiff's expectation were the only aim of the system of remedies, it would be impossible to say why, for example, that system requires mitigation by the plaintiff rather than simply allowing the plaintiff to let his consequential losses mount up, for either would protect the plaintiff's expectation. The same could be said of all the choices of remedies which flesh out the preference for compensation over literal enforcement.<sup>149</sup> To obtain a basic explanation of the system of remedies, one must see that *Robinson v. Harman* itself expresses the two rules set out by Andersen, and together these rules articulate the cooperative project of joint cost minimization within a contractual framework.

The immediate distinctness of the parties to a contract is recognized in the first rule in *Robinson v. Harman*, indicating a general privileging of the plaintiff's over the defendant's interests. The ultimate cooperation of those

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146. *Robinson v. Harman*, (1848) 1 Ex. 850, 855. Cf. RESTATEMENT (SECOND) OF CONTRACTS § 344(a) (1981) ("[H]is interest in having the benefit of his bargain by being put in as good a position as he would have been in had the contract been performed . . ."); U.C.C. § 1-305(a) (2004) ("[T]he aggrieved party may be put in as good a position as if the other party had fully performed . . .").

147. *Robinson*, (1848) 1 Ex. at 854–56.

148. *Id.* at 851.

149. See generally E. Allan Farnsworth, *Legal Remedies for Breach of Contract*, 70 COLUM. L. REV. 1145 (1970).

parties, both within the instant contract and in the economy over time, is recognized by the second rule. If one looks only at the first rule, focusing solely on the protection of the plaintiff's interests, the law of compensatory damages is inexplicable, or explicable only as seriously defective. It is therefore not surprising that the characteristic shortcoming of insistence upon the performance interest is that it cannot even see the existence of the second rule, except indirectly as defects in the system of remedies. It is a shortcoming of relational theory that it does not see that the second rule, though giving an incentive to breach, is basically cooperative.

In a number of my papers on this topic seeking to demonstrate why these two rules have been developed, and in particular why the second complements the first, I have, at considerable risk of exposing myself to ridicule, quoted a passage from one of John von Neumann's papers which have proved to be the foundations of modern computing, which I attempted to read when trying to come to terms with game theory. I quote it once again:

Error is viewed . . . not as an extraneous and misdirected or misdirecting accident, but as an essential part of the process under consideration—its importance . . . being fully comparable to that of the factor which is normally considered, the intended and correct logical structure.<sup>150</sup>

Much of von Neumann's paper is incomprehensible to me, but insofar as I understand the matter, one of von Neumann's contributions to the conceptualisation of computing problems was to recognize that error is ineliminable,<sup>151</sup> and the goal of eliminating error from calculation was illusory. One should first be aware of this, and so not put excessive faith in one's results, and then try to manage the inevitable failure. In computing, von Neumann's basic strategy was to duplicate the calculation on various computers (or parts of computers) and work from some sample of the multiple results.

Without wishing to put any weight on what is intended purely as a heuristic device, I submit that an analogue to this happens in the market economies. It is obvious that in those economies, composed of countless numbers of exchanges of varying degrees of complexity, dealing with those inevitably occurring contracts in which one party finds his costs during

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150. John von Neumann, *Probabilistic Logics and the Synthesis of Reliable Organisms from Unreliable Components*, in *AUTOMATA STUDIES* 43 (C.E. Shannon & J. McCarthy eds., 1956).

151. The mechanical reliability of the computing machines available to von Neumann was very much poorer than that of contemporary computers, but the basic point still holds, of course.

performance growing in an unanticipated way (telling him he made a mistake (in the lay sense) by agreeing to this contract), is a major problem. The mechanism for handling this problem is central to the efficiency of the market economy.<sup>152</sup> The fundamental mechanism is adjustment of obligations by the parties without recourse to legal action, but this is encouraged by limiting the extent to which performance can legally be insisted upon in the way we have seen. It is breach that is most important in setting this limit. Breach allows flexibility into the system of exchanges, allowing parties relief from unanticipatedly expensive obligations when further performance would merely be wasteful as the plaintiff can be compensated in damages. In this sense, *the major function of the law of contract is to allow breach*, but on the right occasions and on the right terms; in essence, on terms which encourage plaintiffs to cover in the knowledge that the defendant will compensate lost net expectation. This is to say, properly regulated breach, breach which does involve adequate compensation, is normative contractual action.

All this, of course, assumes that it normally is possible to take cover, but for commercial parties this normally is possible because the market economies are characterized by the ready availability of goods in competitive supply, including a margin of excess capacity which allows a buyer faced with breach to take cover. This margin functions *inter alia* as the space in which inevitable misallocations of resources through contract are adjusted through breach, or adjustment by the parties which makes it unnecessary for the party experiencing difficulty to breach. Much

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152. A comparison with the extreme rigidities characteristic of the centrally planned command economies is useful. In such economies an analogue to specific performance played the major role as a remedy for failure to comply with obligations under the plan because satisfaction of the plan was the goal of economic action. See Bernhard Grossfeld, *Money Sanctions for Breach of Contract in a Communist Economy*, 72 YALE L.J. 1326, 1327 (1963) ("The plan holds a central position in the East German economy. It expresses the governmental economic policy and fixes . . . . The function of the contract, in turn, is to implement in detail the directives of governmental policy as expressed in the plan." (citations omitted)); Wang Liming, *Specific Performance in Chinese Contract Law: An East-West Comparison*, 1 ASIA PAC. L. REV. 18, 18 (1992) ("Specific performance has a particularly significant role in the law of contract in the People's Republic of China (PRC) because it contributes to the implementation of the state plan."). Of course, as much as in any system, obligations were entered into under imperfect information and with limited computational power, and so their performance was subject to unexpected rises in costs. Though a whole legion of semi-illicit devices for modifying the plan would seem to have arisen (bribes to those who held scarce goods, lying about plan fulfilment, etc), the absence of a general possibility of an analogue to breach to deal with these rises would appear to have caused an inflexibility which was a major weakness of these economies. See generally JANOS KORNAI, *THE SOCIALIST SYSTEM* (1992).

economic theory which views "excess capacity" in the economy as a sign of malaise simply fails to take onboard this vital function of such capacity in making the taking of cover widely possible.<sup>153</sup> This mistake is greatly exaggerated by legal theories of the performance interest, which simply have no inkling of the economic difficulties involved in their pursuit of general literal enforcement, which would require the terms of agreement so often to be right as to eliminate or greatly reduce the necessity of breach. This is a foolish blanket response to the existence of bounded rationality which will fail.

The point of relevance to us is that cover is both efficient and cooperative in a way that undercuts the typical opposition of these qualities. In circumstances when the plaintiff can be compensated in damages, cover obviously is efficient, for insisting upon anything else would be to satisfy the plaintiff's expectation at a higher cost to the defendant than the cost of the cover, and what would be the point of that? The breach is efficient in this case because it minimizes *the defendant's* loss. But this efficiency emerges only because the plaintiff cooperates by taking cover. Allowing the defendant to breach and placing the burden of mitigation on the plaintiff enlists the plaintiff's cooperation in dealing with the defendant's problems, one aspect of this cooperation being that it makes legal action unnecessary in cases where compensation is adequate. In this way, the "efficient breach" that leads to cover in order to minimize the plaintiff's and the defendant's loss is, I suggest, the fundamental provision giving an incentive to cooperation in contract.

If my suggestion is accepted, much of the empirical evidence, such as we have it, about contracting, becomes more readily reconcilable with the properly understood law than is often supposed. If the most detailed formulation of the relational theory is due to Macneil, the arguments that have made the necessity for an alternative theory to the classical law are largely due to Macaulay (and his colleagues at Wisconsin), whose finding of "non-use"<sup>154</sup> made the classical law seem so irrelevant that, as we all know, when Gilmore proclaimed its death, he named Macaulay the executioner.<sup>155</sup> The essential import of Macaulay's conception of nonuse is that the actual conduct of business, and particularly the resolution of

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153. JOHN M. CLARK, *COMPETITION AS A DYNAMIC PROCESS* 81 (1961).

154. Stewart Macaulay, *The Use and Non-use of Contracts in the Manufacturing Industry*, 9 *PRAC. LAW.* 13, 14 (Nov. 1963).

155. See GRANT GILMORE, *THE DEATH OF CONTRACT* 113 n.1 (2d ed. 1995) ("Professor Stuart Macaulay . . . is no doubt entitled to rank as Lord High Executioner of the Contract is Dead School.").



disputes, does not rely on formal legal provisions so much as informal, nonlegal understandings.<sup>156</sup> But in the typical business situation in which failure to deliver a satisfactory generic good is accompanied by a ready market in that good, then nonuse is exactly what one would expect, not because of defiance of the legal rules, but because those rules prescribe the taking of commercial cover, rather than pursuit of a legal remedy in the sense of a remedy which actively involves lawyers.<sup>157</sup> Equally, other apparently lenient responses to breaches, such as allowing repair or (rescheduling) redelivery when complete rejection was possible, can readily be explained as sensible responses to the limited extent to which the plaintiff, even if he or she pursued the formal remedy, would actually find that it took him any closer to literal enforcement of the defendant's primary obligations.

I hope to have at least plausibly advanced the hypothesis that, properly understood, parties to relatively simple contracts relying on standard remedies based on the expectation principle, those contracts which Macneil would call "discrete,"<sup>158</sup> typically have recourse to the "remedy" of what I have elsewhere called "forbearance"<sup>159</sup> when faced with a breach, not because of nonuse as it is normally understood but because the remedies point them in this direction. This is to say, the market apparently works automatically in these cases.<sup>160</sup> There can be nothing so certain as that this

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156. See Stewart Macaulay, *Non-Contractual Relations in Business: A Preliminary Study*, 28 AM. SOC. REV. 55, 58 (1963) ("Businessmen often prefer to rely on 'a man's word' in a brief letter, a handshake, or 'common honesty and decency'—even when the transaction involves exposure to serious risks."). Though my account of the operation of the law of remedies substantially differs from that of Macaulay, which worries me, and is, as I have said, critical of parts of his work, which worries me even more, I have gained great help from his analysis of the "compromises" which are integral to Fuller's conception of the practical quantification of the reliance interest. See generally Stewart Macaulay, *The Reliance Interest and the World Outside the Law Schools' Doors*, 1991 WIS. L. REV. 247. My views on Macaulay generally will appear in David Campbell, *What Do We Mean By the Non-use of Contract*, in STEWART MACAULAY AND CONTRACTS SCHOLARSHIP (W. Whitford et al. eds., forthcoming 2012).

157. Professors White and Summers believe that the dearth of cases on U.C.C. § 2-712 makes it difficult to say with certainty how important it is. 1 JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE, sec. 6-4 n.1 (5th ed. 2006). I am suggesting that it is of the first importance, but this is reconcilable with the views of White and Summers because it is a rule which works so well it does not lead to litigation. My suggestion cannot explain the dearth of cases on the baneful § 2-713. Cf. *infra* note 174 (discussing § 2-713).

158. Ian R. Macneil, *Economic Analysis of Contractual Relations: Its Shortfalls and the Need for a "Rich Classificatory Apparatus"*, 75 NW. U.L. REV. 1018, 1025-37 (1981).

159. HARRIS ET AL., *supra* note 32, chs. 1-2.

160. Oliver E. Williamson, *Transaction-Cost Economics: The Governance of Contractual Relations*, 22 J.L. & ECON. 233, 259 (1979) ("The reason why Macaulay

is not properly understood by the parties, which is an unsurprising state of affairs when the position is not properly understood by most of the parties' advisers; but forbearance is, I submit, the normal case. Revising our understanding here will require not only a readjustment of our view of the substantive law, but, even more, a readjustment of our view of the practical use of that law. We have seen that deliberateness is a ground on which the appropriateness of Section 39 disgorgement is assessed, and that deliberateness is a questionable term. The problem arises, I submit,<sup>161</sup> because "deliberateness" in this respect need not indicate bad faith. Rather, even on current understandings, it could indicate a good faith party being aware of his *decision* to breach, rather than failing to acknowledge responsibility by believing that further performance is "impossible." In Posner's widely quoted words: "[e]ven if . . . breach is deliberate, it is not necessarily blameworthy,"<sup>162</sup> for the deliberateness may just follow from clarity of thought. I would go further and say that, on the understanding I am seeking to put forward, deliberateness *should* be viewed positively, as consciousness of seeking cooperation from the potential plaintiff.

The vast majority of disputes are settled by direct negotiations between the parties in which compromises are reached in the light of all the factors which they consider relevant.<sup>163</sup> The efficiency and therefore legitimacy of breach, the value of a continuing relationship or of possible future business, or, more widely, of a commercial reputation, as opposed to the one-shot value of pursuing litigation most ruthlessly, must all be weighed.<sup>164</sup> I have described the potential plaintiff who, after breach, does not seek a formal remedy, as "forbearing" from seeking a remedy in order to indicate that his decision not to seek the remedy does not take the form of self-conscious cooperation but of forbearance from seeking what, to the extent they

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observes so few litigated cases in business is because markets work well for nonspecific transactions, while recurrent, nonstandard transactions are governed by bilateral or unified structures." (citations omitted). On nonstandard transactions, see *infra* Parts VII–VIII.

161. See HARRIS ET AL., *supra* note 32, at 19 ("Even if . . . breach is deliberate, it is not necessarily blameworthy, for the deliberateness may just follow from clarity of thought." (citations omitted)).

162. Patton v. Mid-continent Sys. Inc., 841 F.2d 742, 750 (7th Cir. 1988).

163. See Macaulay, *supra* note 74, at 465–71 (stating that "lawyers settle most [breach cases] before courts reach final decisions" and that relevant considerations include the fact that "[o]ne must pay for one's own lawyer, and one must win enough to offset all the costs of the endeavor" and "such considerations as the immediate need for money").

164. See generally James Shanteau & Paul Harrison, *The Perceived Strength of an Implied Contract: Can It Resist Financial Temptation?*, 49 ORGANIZATIONAL BEHAV. & HUM. DECISION PROCESSES 1 (1991).

believe in *pacta sunt servanda*, they must believe is an ability to compel the defendant to perform. This is a giving up of what the potential plaintiff perceives, however incorrectly, to be a right, for pragmatic reasons. For though the overwhelming weight of evidence is that disputes will be settled out of court by compromise, the present understanding of remedies encourages a "vindication of rights" mentality in the conduct of litigation.<sup>165</sup> The most aggravated form this takes, now deplored and intended to be corrected by the last major set of reforms of civil procedure in England and Wales, is the tendency of commercial litigation to

degenerate into an environment in which the . . . process is too often seen as a battlefield where no rules apply. In this environment, questions of expense, delay, compromise and fairness may have only a low priority. The consequence is that expense is often excessive, disproportionate and unpredictable; and delay is frequently unreasonable.<sup>166</sup>

To this I would add that an otherwise valuable business relationship subjected to the strains of the "resolution" of a dispute in this way is unlikely to survive that resolution,<sup>167</sup> which would appear to be a very substantial and largely unjustifiable cost which civil litigation imposes on business.

Businesses can, and perforce do, avoid these costs by eschewing litigation conducted in this way, but the vindication mentality casts its pall over post-breach negotiations in which reference to the contract takes the form of exchanges of surrenders of adversarially asserted claims. The only general present corrective to this seems to be the advice one imagines is given very commonly indeed, that the law in practice falls short of the law in books (in which the client would get his supposed full deserts), which is a very unsatisfactory position indeed.<sup>168</sup> Self-consciousness of the cooperative element of contract is a necessary condition for improving the basic quality of advice in this regard. Parties who are aware that the

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165. See HUGH COLLINS, *REGULATING CONTRACTS* 350–55 (1999) ("Settlement is the preferred outcome of the parties in most contractual disputes, not some formal vindication of contractual rights based upon a narrow and partial interpretation of expectations.").

166. LORD WOOLF, *ACCESS TO JUSTICE (INTERIM REPORT)* 7 (1995), available at <http://webarchive.nationalarchives.gov.U.K./+http://www.dca.gov.U.K./civil/interim/chap3.htm>.

167. See COOPERS & LYBRAND, *LITIGATION SUPPORT* 1 (C.J. Lemar & D.R. Chilvers eds., 3d ed. 1995) (stating "litigation will almost certainly terminate any future business relationship").

168. See generally Immanuel Kant, *On the Common Saying: That May Be Correct in Theory But It Is of No Use in Practice*, in *PRACTICAL PHILOSOPHY* 273 (1996).

expectation principle encourages cooperation would not have to learn this by the expensive pursuit of vindication through litigation which is almost always frustrated by settlement, which indeed is the unsatisfactory way in which the ubiquity of compromise between good faith parties is currently made known to those parties.

I do not for a moment want to deny that the expectation principle (and certainly Fuller and Perdue's statement of it) is in need of reform. But I do think that its basic thrust is correct, and that what has misled business parties and (neo)classical contract scholars and practitioners is that they think primary obligations *should* be performed, when it is always questionable whether they should. Of course, a party who breaches at all frequently rightly will go out of business. He will repeatedly waste his own reliance and fail to realize his own expectation, as well as be liable for the reliance and the expectation of the plaintiff. But the necessity of allowing for business failure does not tell us how to deal with the relatively low incidence of breach inevitably sustained by all continuing businesses as, indeed, a cost of doing business in conditions of bounded rationality. Self-consciousness of the cooperation that actually underlies the properly understood law and practice of breach would allow the displacement of the always frustrated taste for litigation based in the vindication of rights mentality to be replaced by a taste for settlement based in an acknowledgement that the adequate form of self-interest always acknowledges a role for cooperation. It certainly would be singularly unwise to generally strengthen the plaintiff's ability to adopt the vindication mentality.<sup>169</sup>

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169. Of course, as the restitutionary logic leads in this direction, one finds abstract arguments for pure vindication remedies now being made. *E.g.*, David Pearce & Roger Halson, *Damages for Breach of Contract: Compensation, Restitution and Vindication*, 28 OXFORD J. LEGAL STUD. 73, 73 (2008) ("Vindication describes the making good of a right by the award of an adequate remedy. . . . [Vindicatory damages] are neither compensatory nor restitutionary, neither loss-based nor gain-based: they are a rights-based remedy."). The predictability of this development does not detract from its tedious circularity. Because breach is a wrong even when it leads to no substantial loss, it is now argued that we need remedies which effectively vindicate cases which previously would have led to a nominal award, with the plaintiff probably effectively being punished for wasting the court's time by an adverse costs award. *Id.* at 97–98. But surely one can see that it is the persuasive definition of the "wrong" that is doing all the work here, when what is needed is inquiry into the nature of a "wrong" that the law does not normally seek to remedy. U.S. scholars will find it difficult to appreciate just how far many Commonwealth academic and judicial contributors to the Birksian argument are unaware of the progress that has been made in this inquiry in the American literature. *See generally, e.g.*, Webb, *supra* note 130.

The bad man does not, I think, turn out to be so bad on this understanding. He undoubtedly is oriented to maximization, but, properly understood as part of a welfare-enhancing economy, this orientation is incompatible with disregard of others' interests, and is not individualistic in any atomistic or solipsistic sense. He pursues his self-interest, but in a way which intrinsically recognizes the interests of others. The bad man recognizes that peaceful, proportionate exchange is the legitimate means of acquiring the property of others, and carries out that exchange by means of a law of contract which involves sophisticated cooperation with others. It is cooperation within the law of remedies that concerns us here, but we are becoming conscious that the law of contract sets up cooperation throughout its doctrines, and that this cooperation is essential for the bad man to realize his own interests.<sup>170</sup>

#### *VI. Applying the Relational Theory of Breach to Section 39*

The attack on breach that underlies the Birksian argument and Section 39, far from articulating a superior moral position, articulates a commitment to the vindication of the plaintiff's rights which is inferior in its moral quality and its economic effects to the cooperation articulated in the expectation-based law of remedies. This commitment is not unbridled, because fine scholars such as Kull and Roberts see that a bridle is necessary.<sup>171</sup> But their focus on the limitation of the restitutionary remedy is, we will see, merely ad hoc, because their basic principle is a conception of breach as a wrong which, as I have said, is itself wrong.

It will be recalled that the definition of a "profitable" breach given in Section 39 tells us that "[p]rofits from breach include saved expenditure and consequential gains."<sup>172</sup> Though it is "consequential gains" that are at the heart of the usual concept of efficient breach, in which the defendant

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170. For my own writings on the relational constitution of agreement, see David Campbell, *The Relational Constitution of the Discrete Contract*, in *CONTRACT AND ECONOMIC ORGANISATION: SOCIO-LEGAL INITIATIVES* 40 (David Campbell & Peter Vincent-Jones eds., 1996); David Campbell & Hugh Collins, *Discovering the Implicit Dimensions of Contract*, in *THE IMPLICIT DIMENSIONS OF CONTRACT* 25 (David Campbell et al. eds., 2003); David Campbell, *The Relational Constitution of Contractual Agreement*, in *THE SOCIAL INSTITUTIONS OF CAPITALISM: EVOLUTION AND DESIGN OF SOCIAL CONTRACTS* 38 (Pursey Heugens et al. eds., 2003).

171. *Supra* notes 40–43 and accompanying text (noting the need to limit the disgorgement remedy).

172. RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39(3) (2011).

breaches in order to obtain an extra gain, there can be no principled way from the restitutionary perspective of distinguishing between this maximizing breach and what I have called the minimizing breach which results in "saved expenditure." Kull is to be congratulated for seeing that this problem exists, which saves me from being obliged to argue the point, as has been necessary in respect of the Commonwealth literature. But in Comment f to Section 39, Kull goes on to argue that:

[T]he requirement that an opportunistic breach be *profitable* eliminates most instances of breach. The basic calculation of compensatory damages makes it highly unlikely, in any transaction for which there are market-based substitutes, that the gain to the defendant as a result of the default will exceed the injury to the plaintiff from the same cause.<sup>173</sup>

With respect, this is quite wrong, and perhaps the best way to show this is by some examples that are intended to be absolutely characteristic of a normal breach of a sale of generic goods when cover is available and the case would be governed by UCC § 2-712.<sup>174</sup> The defendant agrees to deliver a consignment of standard steel to the plaintiff for a price of \$1 million. The factory in which he intended to make the goods is then destroyed by fire, and, were he to try to perform his obligations by rescheduling his production in order to still make the goods himself, it would cost him \$1.5 million to do so. These goods are available on the market for \$1.1 million. The rational thing to do is to breach. On compensatory damages rules, the defendant will be liable for \$100,000 market damages, that sum representing, of course, the excess of the plaintiff's payment to a third party seller over the contract price, and it is rational for the defendant to breach because this is smaller than the \$500,000 extra expense which actual performance would cause him. It is overall efficient that he do so because, whilst the defendant saves, the plaintiff suffers no loss of expectation. I can see nothing in the wording of Section 39, or in the previous restitution literature on profits from breach of contract, including that of Kull himself, to see why the \$400,000

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173. *Id.* § 39 cmt. f (emphasis in original).

174. I will simply ignore the way that the availability of market damages in the absence of cover under UCC § 2-713 contradicts my argument. Section 2-713 (and the corollary seller's remedy under § 2-708(1)) contradicts my argument because it contradicts the basic aim of contract damages, incorporated into the UCC under § 1-305, and is, in my opinion, an indefensible anomaly for which no satisfactory rationale has ever been provided. I will not argue it here but, in my opinion, the only plausible explanation of § 2-713 is in terms of the irrational persistence of conventional thinking of the sort that § 2-712 was meant to render obsolete.

(\$500,000–\$100,000) is not "saved expenditure" following from the wrong of breach, and subject to disgorgement. Of course, the breach would also have to be deliberate under Section 39(2)(a) and damages would have to be inadequate under Section 39(2)(c). But, in this context, deliberate is likely to mean only that the defendant was able competently to assess his position and not panic, and I will not say anything else about this dreadful red herring. But the English case law allows us to say something about the inadequacy of damages.

Section 39(2)(c)(i) tells us that "damages are ordinarily an adequate remedy if they can be used to acquire a full equivalent to the promised performance in a substitute transaction."<sup>175</sup> In Comment c, Kull adds:

As a general rule, damages are an adequate remedy only if they can be used to replace the promised performance in a substitute transaction. Where such a replacement transaction is available, the promisee's remedy in contract damages makes disgorgement unnecessary; and the promisor's breach will not be opportunistic by the [Section 39] definition.<sup>176</sup>

One can perfectly well see what Kull is driving at here, and why, by ruling out the normal case I am asking us to consider, he thinks this will mean that Section 39 will be "distinctly rare."<sup>177</sup> But this is a terrible case of hoping to have one's cake and eat it too. The damages *are* adequate in these cases, but only if the plaintiff's protected interest is an expectation that is quantified without reference to the gains of the defendant. But surely Kull cannot be maintaining that this is how we should view the interest of the plaintiff. If so, what is R3RUE's treatment of breach as a wrong about?

There is a particular case that lays bare the egregious inconsistency. This is the case where the plaintiff's damages are nominal; the case that, as

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175. RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39(2)(c)(i) (Tentative Draft No. 4, 2005). Citation to Tentative Draft No. 4 was necessary here because the wording of Section 39 changed slightly between the initial writing of this Article and the final iteration of the Restatement. However, while the wording may have changed, the essential concepts remain the same. See RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39(2) (2011) ("A case in which damages afford inadequate protection to the promisee's contractual entitlement is ordinarily one in which damages will not permit the promisee to acquire a full equivalent to the promised performance in a substitute transaction."); *id.* § 39 cmt. f ("[T]here is no opportunism and no claim under this section if a damage remedy affords adequate protection to the promisee's contractual entitlement, by allowing the promisee 'to acquire a full equivalent to the promised performance in a substitute transaction.'" (citations omitted)).

176. RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39 cmt. c (Tentative Draft No. 4, 2005).

177. *Id.* § 39 cmt. a.

I have said, has been behind most of the English cases between *Wrotham Park* and *Blake*. Let us imagine that, in our example, the steel was available on the market for \$1 million. The defendant will *a fortiori* wish to breach, but things are very difficult from the restitutionary perspective. The plaintiff now has no loss at all on compensatory rules, and this is just when the plaintiff's being confined to nominal damages is regarded as unjust, so it is impossible to see why this will not generate a restitutionary claim which completely undermines all attempts to keep the restitutionary remedy within sensible bounds. It is not good enough to say that he really has no loss, for even if we establish that the plaintiff really is compensated by nominal damages because he did not, in fact, suffer a substantial loss, the defendant has not had to pay for the hypothetical release from his obligation to deliver by which he made a saving of \$500,000. The plaintiff is compensated for normal expectation loss but not paid a sum in addition to this for release, and the defendant is making profits by the wrong of breach. (This is ultimately why the hypothetical release or loss of opportunity to bargain concept is also so unsatisfactory.) It is utterly incoherent to fail to maintain a restitutionary claim here, and one could not do so consistent with the English restitution cases.

And once this is allowed, then it equally applies if the market price were \$1.1 million, as we originally supposed, for, as the \$100,000 is the plaintiff's lost expectation, the defendant did not pay for the hypothetical release which allowed him to make a net saving of \$400,000 in that circumstance. It is, I submit, impossible to distinguish these two cases on the ground that in one of them compensatory damages are nominal; the logic of disgorgement of wrongful profits must apply to both (and if it applied to merely one it would still be completely unacceptable). It is principally for this reason that I have called the *Blake* argument "ridiculous in itself" in earlier work, because if the defendant has to pay for release in these cases, commercial law as we have it will collapse.<sup>178</sup>

### VII. Choice over Levels of Precaution

Reflection on the most standard case of breach shows, then, that to hold that the aim of remedies for breach of contract should be the prevention of breach is quite wrong and rests on a misunderstanding of the working of market exchange. Fortunately, the intentions of commercial

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178. HARRIS ET AL., *supra* note 32, at 267.



parties reflected in the common law of contract are too sophisticated to be formed by reference to this goal. Faced with the inevitability of breach as a practical commercial reality, parties have not fruitlessly attempted to eliminate it, but have contracted on terms which set the optimal level of precaution against it, and their wisdom is institutionalized in the common law of expectation-based remedies.<sup>179</sup> This would be swept away by the current criticism of that law that informs Section 39, which therefore cannot respect the intentions of the parties. The most telling criticism of the performance interest and restitutionary damages is that the stress they place on performance would not be able even to be pursued as a goal unless freedom of contract in respect of choice of remedies were abolished.

The institutionalization of economic choice in freedom of contract requires the law to refrain from imposing its own terms into contracts, and instead to strive to give effect to the intentions of the parties. That this requires, for example, ensuring that the price of goods, such as the \$1 million for our steel, is the product of the parties' voluntarily agreed bargain, is widely understood (though this is a much more complex matter than is usually appreciated, involving the state in much more than merely refraining from setting prices).<sup>180</sup> What is much less widely understood is that freedom of contract also requires that the terms of the contract stipulating liability should also be the product of the parties' agreement, for this is essential to rational price formation and the efficient functioning of markets.<sup>181</sup> For the "fully contingent" price of goods includes not merely the cost of, as it were, the physical production of the goods, but also, *inter alia*, the cost of bearing the liability which the parties undertake by agreeing to the contract, with its latent secondary obligation to provide a remedy.

Our argument now requires us to look at one aspect of the way that compensatory damages work as the default rule in the developed system of commercial law. The default remedy is, of course, implicitly stipulated as the remedy which will apply in the absence of explicit agreement otherwise.

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179. See Craswell, *supra* note 142, at 650 ("To the extent that the noncompensatory remedies require a breaching defendant to pay more or less than the plaintiff's actual injury, they will induce an inefficiently high or low level of precautions.").

180. See discussion *infra* Part X (noting the role of the state in the system of contracts).

181. See Richard A. Epstein, *Beyond Foreseeability: Consequential Damages in the Law of Contract*, 18 J. LEGAL STUD. 105, 108 (1989) ("Damage rules are no different from any other terms of a contract. They should be understood solely as default provisions subject to variation by contract. The operative rules should be chosen by the parties for their own purposes, not by the law for its purposes.").

In the common law, these implicit terms are the product of the institutionalization of commercial practice in cases, guided by precedent and amended by statute. Subject to some significant (by no means always defensible) exceptions which need not be mentioned here, the commercial law does not make it mandatory that compensatory damages are the remedy for breach, but allows the parties to "contract out of" or "oust" this default rule by stipulating their own "bespoke" rule governing remedies.

We can see the significance of this if we imagine that the steel in our example was not a generic good readily available in competitive supply, but a specially commissioned specific good with special qualities, and no substitute was readily available for this steel. The seller's failure to deliver could not, in these circumstances, be met by covering, and breach would threaten the buyer with consequential loss. As Kull and Roberts insist as part of their cases for Section 39, the causation rules, particularly the requirement of certainty, could well pose the plaintiff serious difficulty in obtaining compensatory damages in such a case. One might well concede that the buyer's ultimate net profit was, except in unusual circumstances, going to be positive, but quantification problems may prevent the full compensation of the plaintiff, certainly in his own opinion. The very same causation rules which allow compensatory damages to work so well in the relatively easy quantification of market damages make those damages generally inappropriate to the quantification of "idiosyncratic" losses of this nature. The potential plaintiff who negotiates in ignorance of this can well be left with a very substantial uncompensated loss.<sup>182</sup>

A competent potential plaintiff faced with possible uncompensated loss under the default rule will (having reviewed other possibilities such as obtaining insurance from a third party) negotiate to oust the default rule and replace it with one which imposes a liability on the potential defendant in which the potential plaintiff has confidence. Within the limits imposed by the law, he may, for example, require the potential defendant to post a bond which will be forfeited on breach, or stipulate a fixed sum which the potential defendant will pay on breach only remotely related to what the other party would have had to pay as compensatory damages, or try to make compulsory performance the remedy regardless of whether the special case normally required for this could have been made out. There are many other

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182. A good English example, in which the issues were thoroughly canvassed by the Court of Appeal and the House of Lords, the latter reversing the former, is *Co-operative Ins. Soc. Ltd. v. Argyll Stores (Holdings) Ltd.*, [1996] Ch. 286 (C.A.); [1998] A.C. 1 (H.L.(E.)). Though I will not go into this here, an interesting, significantly different position has been taken in the hybrid civilian and common law system of Scotland.

possible devices for securing "real," rather than merely "legal," remedies, the devising of which constitute a most important branch of advanced commercial law.

The device which concerns us here, which certainly is open to the potential plaintiff, is to stipulate restitutionary rather than compensatory damages as the remedy. But, of course, to get this into the contract, the potential plaintiff has to get the potential defendant to agree to it, and herein lies the problem for the potential plaintiff, and the source of the wisdom of commercial parties institutionalized in the default rule. For the reason we have seen, compensatory damages are normally cheaper for the defendant than restitutionary damages (or compulsory performance), and in negotiations in which this is an issue, *ex hypothesi* this is so, otherwise the defendant would be indifferent between these remedies, and agreement of a remedy would be straightforward. The potential plaintiff may wish to get the extra security of primary performance that comes from making restitutionary damages the remedy, but the potential defendant will want payment for this as he is incurring extra liability, and so will have to take extra precautions against breach, or obtain extra insurance, etc. He may, in our steel example, contract with two suppliers for the necessary iron ore, thereby greatly reducing the chance of failure of supply, even though he will incur avoidable costs in, for example, warehousing the consignment of ore he does not use making the steel for this contract. The range of means of taking extra precaution are very large, but, the point is, all will impose extra cost. Though the physical steel will be the same, the price will be higher if restitutionary damages are the remedy because the liability will be higher.

Now, if the risk of idiosyncratic loss is high, the potential plaintiff may pay the higher price for steel, because the extra security, and ultimately extra precaution, will be of value to him. But when the exposure is to merely market damages in the normal way, the potential plaintiff will not pay the extra price, because the extra security, and ultimately extra precaution, has no value to him, as he can obtain a satisfactory substitute for undelivered goods on the market. In our steel example, if the steel is generic steel available on the market, then adequate security is provided by the ready availability of a substitute, and extra precaution is pointless. Depending on the extent of his exposure to idiosyncratic loss, the potential plaintiff will be prepared to pay for extra precaution, and negotiation between the parties will fix the optimal level of precaution. In extremely high value contracts involving a high level of exposure to idiosyncratic loss, such as if special steel was required for shielding a nuclear power

installation, the potential plaintiff may be prepared to pay for as near as possible absolute precaution, because this is the optimal level of precaution. But in normal cases, in which cover is readily possible, such precaution would be a senseless waste for which no-one would voluntarily pay, for the optimal level of precaution is much lower.

The serious mistake made in the current criticisms of the law of remedies is to think that the law is unilaterally generous to the defendant. As I have claimed,<sup>183</sup> it is nothing of the sort. It is as generous (if this terminology may be used) to the defendant as the plaintiff and defendant have agreed. The plaintiff can avail himself of a lower price if he contracts on the basis of compensatory damages which effectively require him to cooperate in dealing with the mistaken agreement by normally providing his own remedy by taking cover, which keeps the defendant's liability, and therefore the price he will agree to, low. If the plaintiff wants to impose heavier liability on the defendant, he can do so by negotiating with the defendant to do so, and paying for this.

We have seen that, in discrete contracts, a form of cooperation which seems automatic arises in dealing with the consequences of breach. This automaticity is possible only because cover is the standard rational response in simple cases. But in more complex cases, this standard response will not work, and cooperation in these cases takes (or should take) the more conscious form of explicit negotiation between the parties.<sup>184</sup> I will place this "spectrum" of forms of cooperation in the context of the relational theory in the next Part of this Article. For now we should note that the expectation-based law of remedies establishes a sophisticated cooperative framework within which competition and choice over the terms of the contract stipulating the remedy takes place, and an order of optimal levels of precaution emerges.

The extent of the error of seeing the current rules as unilaterally generous to the defendant can be fully appreciated if we speculate on the consequences of changing the law to make disgorgement damages the default remedy. The potential defendant contracting on this basis would incur the higher level of liability and so would have to charge a higher price

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183. See *supra* text accompanying note 143 (discussing the need for "joint-cost minimization").

184. See David Campbell & Donald Harris, *Flexibility in Long-Term Contractual Relationships: The Role of Co-operation*, 20 J.L. & SOC'Y 166 (1993) ("[W]hat the evidence shows . . . to be the case, is that failures under [long-term contract] circumstances lead . . . to extra-legal strategies to keep the long-term relationship alive in all but the most acute circumstances.").

for the goods. Competition would quickly lead to sellers offering to sell on terms which explicitly ousted this default and replaced it with a bespoke compensatory damages clause, and, in the normal case, buyers would contract on these cheaper terms. There would be the extra transaction cost of having to contract away from a default which is unsuitable in the normal case (which is why compensatory damages now are the default), but the ultimate result would be the same. The only way to prevent this would be to make the disgorgement remedy mandatory, that is to say, impose it on the parties and make it impossible for them to contract out of that remedy.<sup>185</sup> The contradiction between the abstractly legal criticisms of the current law of remedies and the law of contract which institutionalizes economic choice as freedom of contract could not be more marked.

*VIII. Why Cases Like Wrotham Park Arise, and How to Deal with Them*

We are now in a position to see why cases like *Wrotham Park* arise, and to see how they should be dealt with. In *Wrotham Park*, the plaintiff clearly believed that the restrictive covenant would bind the defendant to building only within the lay-out plan.<sup>186</sup> In this, he was wrong, and, of course, this is why, as we have seen, the Court felt that "justice [would] manifestly not have been done"<sup>187</sup> by an award of nominal compensatory damages. In all the subsequent discussion of this case, it has been accepted that the Court was right, and Kull is so sure of this that, in Illustration 11 to Section 39, he effectively tells us that Section 39 would endorse total disgorgement of the defendant's profit in *Wrotham Park*, a much better result for the plaintiff than the small partial disgorgement he did obtain.<sup>188</sup>

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185. I think one can fairly say that Birks's thinking over this vital point is so confused that one cannot say what just his position was, and one hesitates to say that he fundamentally misunderstood (freedom of) contract. But there can be no doubt he was prepared to impose "restitutionary rights" by "the operation of law as opposed to the consent of the party enriched." Birks, *supra* note 3, at 44.

186. *Wrotham Park Estate Co. v. Parkside Homes Ltd.*, [1974] 1 W.L.R. 798 (Ch.D.) 799.

187. *Id.* at 815.

188. See RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39 cmt. e, illus. 11 (2011) ("Landowner sells part of his land to Developer for subdivision; Developer agrees to build no more than 100 houses on the property. Developer's covenant to this effect is valid and enforceable by Landowner."). The illustration continues:

Acting in deliberate disregard of his contractual obligations, Developer builds 120 houses. In a subsequent lawsuit between the parties, the court finds that (i) Developer's breach of contract enabled Developer to realize an additional

But this is not right, and, indeed, is a variant of the incorrect understanding of the working of the law of remedies which this Article seeks to address.

I have mentioned that *Wrotham Park* was not decided as a restitution case but on grounds derived from nineteenth century equity jurisprudence, and that the first modern rationalization of the decision was in terms of hypothetical release damages.<sup>189</sup> The first clear English judicial statement of this rationalization was provided by Megarry V.C. three years after *Wrotham Park* in *Tito v. Waddell (No.2)*:<sup>190</sup>

[i]f the plaintiff has the right to prevent some act being done without seeking his consent, and the defendant does the act without seeking that consent, the plaintiff has suffered a loss in that the defendant has taken something for which the plaintiff could have required payment, namely, the right to do the act.<sup>191</sup>

I trust we can now see that, with respect, this is quite wrong. When a potential plaintiff obtains agreement to a clause in a contract, he obtains security against nonperformance of the obligation set out in that clause. But, by default, that security, Holmes has told us, is the security provided by compelling the defendant to pay compensatory damages in the event of breach.<sup>192</sup> By default, a contract does not give the plaintiff "the right to prevent some act being done without seeking his consent";<sup>193</sup> this is precisely what it does *not* do. It allows the defendant to breach without

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\$200,000 profit from the transaction, and (ii) Landowner would have agreed to permit the construction of an additional 20 houses on payment of \$20,000. Landowner's recovery from Developer by the rule of this Section is \$200,000. If Developer's liability in restitution were limited to the \$20,000 that would have been paid in a voluntary transaction, a party disposed to breach in these circumstances would have inadequate incentive to bargain over a release from the covenant.

*Id.* The reason why the recovery was so small in *Wrotham Park* is a good one, but it turns on nineteenth century English equity jurisprudence to such an extent that setting it out here would be inappropriate. It is set out in HARRIS ET AL., *supra* note 32, at 488–94; and Campbell, *supra* note 58.

189. See *supra* note 88 and accompanying text (discussing hypothetical release).

190. See *Tito v. Waddell (No. 2)*, [1977] Ch. 106, 111–13 (finding that although certain mining leases called for the paying of royalties "in trust" to land owners by the government, this did not create a true trust or fiduciary obligation, and with respect to a replanting obligation "that the damages should be more than nominal or minimal").

191. *Id.* at 335.

192. HOLMES, *supra* note 25, at 301 ("[T]he 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. [The law of contract] leaves [the promisor] . . . free to break his contract if he chooses.").

193. *Tito*, [1977] Ch. at 335.

consent, if he will pay for doing so.<sup>194</sup> The whole hypothetical release argument rests on a fallacy; the very one Holmes warned us against.<sup>195</sup>

However, this is not to say that there is no "lost opportunity to bargain." It is just that the lost opportunity does not come at the time of breach. It comes at the time of the original agreement, and really, one should ask, when does one expect opportunities to bargain to arise? A competent party has an opportunity to bargain, for, as we have seen in the previous Part of this Article, with some exceptions, there is nothing to prevent the parties ousting the default and providing for something more appropriate, such as restitutionary damages.

The general reason they do not do this is the reason why this Article is written. Most parties contract, and receive advice to contract, based on literal belief in *pacta sunt servanda*, and, thinking that, by contracting, they get a guarantee of performance of primary obligations; they do not see the necessity of further negotiation to get what they really want. Should they realize they are contracting on the default basis of the Holmesian choice, they would do so. And, of course, a substantial part of being a good

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194. Of course, in *Wrotham Park* there was the possibility of an injunction, and there can be no doubt the plaintiff hurt his own position by failing to pursue this remedy in a timely manner. The issue of the relationship of equitable remedies and restitutionary damages was very thoroughly discussed in a line of real property cases between *Wrotham Park* and *Blake* in which such an equitable remedy might have been sought, but I do not think it fruitful to discuss this particular issue here, though I have examined it at length in HARRIS ET AL., *supra* note 32, ch. 17. In an important sense, the Birksian argument in contract (and even more Friedmann's argument for the performance interest) is a way of avoiding the existing limits on a plaintiff's ability to obtain literal enforcement by making damages to similar effect widely available as of right. See generally Daniel Friedmann, *Economic Aspects of Damages and Specific Performance Compared*, in CONTRACT DAMAGES 65 (Djakhongir Saidov & Ralph Cunnington eds., 2008). But the general problem of denial of literal enforcement when the plaintiff, who in theory could be compensated by a money award, fears damages limited by the causation rules will be inadequate pervades the entire law of remedies for breach of contract, admittedly giving rise to very difficult, in fact in my opinion impossible, balancing problems for the court, HARRIS ET AL., *supra* note 32, pt. 3, only because the law very imperfectly recognizes the general principle of recognizing the defendant's, as well as the plaintiff's, interests. See Campbell, *supra* note 62, at 141 ("[T]he use of restitution to give greater protection to the 'performance interest' in contract generally . . . ignores the countervailing interests of the defendant, principally in having losses mitigated. Were *Blake* carried through it would have the effect of eliminating or reducing the role of mitigation . . ."). In his comments on this Article, Professor Shupack has rightly said that these problems are known in the United States in relationship to cases such as *Jacob & Youngs Inc. v. Kent*, 129 N.E. 889 (N.Y. 1921), and *Peevyhouse v. Garland Coal and Mining Co.*, 382 P.2d. 109 (Okla. 1963). I regard this problem as a large part of the problem of uncompensated loss discussed in this Part of this Article.

195. See Holmes, *supra* note 27, at 462 ("The duty to keep a contract at common law means a prediction that you must pay damages if you do not keep it—and nothing else.").

contract lawyer lies in realizing just this, and dealing with it. Were a construction lawyer who failed to advise his client to provide, say, for binding expert third-party assessment of the costs of late completion, or a commercial lawyer who failed to advise his client to stipulate liquidated damages for failure to deliver a vital, bespoke component, to quote *pacta sunt servanda* to the client left uncompensated after breach by way of explanation of the client's plight, he rightly would be regarded as incompetent. Now, of course, a client who does contract on the basis of *pacta sunt servanda*, only to find how misleading this maxim is, may very well find himself faced with the uncompensated loss under Section 39(2)(c) against which Section 39 is intended to provide. We have seen that uncompensated loss is a serious problem in the law of contract, but it is because, as Professor Coote has said, there is "wide acceptance of the phrase '*pacta sunt servanda*,'" <sup>196</sup> when understanding the law of remedies turns on recognizing there is no such widely accepted practice, <sup>197</sup> and that such loss comes as a shock in *Wrotham Park* cases. The remedy for this is, not to have laws like Section 39, but for parties to see *pacta sunt servanda* for the nonsense it is when taken literally, and deal with the problems themselves.

The main arguments against Section 39 advanced here are that it has no logical or practicable stopping point; that the stress placed on its being exceptional by Kull and Roberts can have little purchase because it is undermined by the very idea that breach is a wrong; that the English case law has shown all this to be the case; and that, with freedom of contract, the parties' typical response to an attempt to make the restitutionary remedy the default would be to contract out of it. We can now see that, in addition, the consequences of granting the restitutionary remedy when the parties have contracted on the basis of a compensatory default rule, and so have not made provision for disgorgement, actually are unwelcome. The plaintiff may well later wish that he had made such a provision, but, the parties having contracted on a compensatory basis, it is effectively an unjustifiable revision of the parties' allocation of the burdens and benefits of the contract to give a remedy on an entirely different basis. This has particularly clearly happened in an English case similar to *Wrotham Park*, which defied as clear a set of rules (based on an express provision of an Act of Parliament)

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196. Brian Coote, *Contract Damages, Ruxley, and the Performance Interest*, 56 CAMBRIDGE L.J. 537, 542 (1997).

197. See Campbell, *supra* note 13, at 272 ("The basic remedy [for breach on contract under English law] is not the compulsion performance, but rather compensation of the claimant by compulsory payment of damages.").



about the interpretation of conveyances of land as it is possible to conceive, in order to give a *Wrotham Park* remedy on terms rather better than were granted in *Wrotham Park* itself.<sup>198</sup> On the interpretation mandated by statute, the conveyance in this case did not even contain a restrictive covenant.<sup>199</sup> But this was no barrier to yet another English Court which was determined to reach "a result which would appeal to the Court."<sup>200</sup> I merely refer U.S. readers to my discussion of this case elsewhere,<sup>201</sup> and turn to the famous case with which they will be familiar which raises the fundamental issue: *City of New Orleans v. Firemen's Charitable Association*.<sup>202</sup>

Leaving aside the importance of this case in the United States, which has led to Kull using it as the basis of Illustration 7,<sup>203</sup> it has played an important part in the development of the Birksian argument in the U.K. Jones brought it to wide attention in an important article<sup>204</sup> published prior to Birks's *An Introduction to the Law of Restitution*,<sup>205</sup> and it had a particular influence on the Court of Appeal hearing of *Blake*, where it lay behind the "skimped performance" ground for awarding the restitutionary damages which, Lord Woolf M.R. told us, "justice surely demands . . . in such a case."<sup>206</sup> But all this has been done despite the fact that the contract was not breached in *City of New Orleans*!<sup>207</sup> Kull, who acknowledges that

198. *Lane v. O'Brien Homes*, [2004] EWHC 303 (QB).

199. *Id.* para. [4].

200. *Id.* at [11].

201. See generally Campbell, *supra* note 58.

202. *City of New Orleans v. Firemen's Charitable Assoc.*, 9 So. 486, 488 (La. 1891) (finding that the failure of the Fireman's Association to maintain the number of employees, length of hose, etc. as required by the contract, was not grounds for any compensation to the city).

203. See RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39 reporter's note d (2011) ("Illustration 7 adopts the facts . . . in *City of New Orleans* . . .").

204. Gareth Jones, *The Recovery of Benefits Gained from a Breach of Contract*, 99 LAW Q. REV. 443, 455 (1983).

205. BIRKS, *supra* note 3, at 344. In Birks, *City of New Orleans* was misunderstood in the common way and taken to be "a type of case in which the test of 'deliberate exploitation' [*Id.* at 326–27] ought to be brought into play, so as to allow recovery of profits against an unscrupulous contract breaker." *Id.* at 334.

206. *Attorney Gen. v. Blake*, [1998] Ch. 439 (C.A.) 458.

207. See *City of New Orleans*, 9 So. at 488 ("From the absence of any averment in the petition that the fires were not extinguished, and from the documents annexed to the petitioner particularly affirming that this condition was performed, we are of opinion that the main purpose of the contract was faithfully executed.").

his illustration "reverses" the result of the case,<sup>208</sup> is unusually acute in seeing this. Kull's illustration reads as follows:

City contracts with firefighter's Association for fire-protection services to be furnished during the ensuing twelve months. The contract specifies the number of men, horses, and wagons to be kept in readiness at specified times and places, and the contract price is negotiated as a function thereof. After the twelve months have elapsed and the full contract price has been paid, City discovers that Association consistently devoted fewer men, horses and wagons to City's fire protection than the numbers required by the contract. Association acted in deliberate breach of its contractual obligations, calculating—accurately as it turned out—that the resources specified by contract were in excess of City's firefighting needs. In consequence, Association saved \$100,000 over the life of its contract with City; while City suffered no increased loss from fire as a result of Association's disregard of the contract specifications. City is entitled to recover \$100,000 from association [under Section 39].<sup>209</sup>

Now, this is an illustration, not an account of the case, and it departs from the case in a number of important ways.<sup>210</sup> Most importantly, in the illustration "[t]he contract specifies the number of men, horses and wagons to be kept in readiness at specified times and places," and by devoting "fewer men, horses and wagons to City's fire protection than the numbers required by the contract [the] Association acted in . . . breach of its contractual obligations."<sup>211</sup> This is not what happened in *City of New Orleans* itself, which involved a contract "to extinguish fires [and] to keep up . . . equipments to a certain standard, so as to insure a faithful performance," which was performed.<sup>212</sup> Now, the City did set out a list of "men" and "equipments," and the defendant did not provide all of these.<sup>213</sup> But the literal provision of the items on this list cannot have been identified to the contract, or the finding of no liability in the case is nonsensical, and to understand the decision in the case it is important to see that the defendant's performance as monitored by the plaintiff seems to have been

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208. RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39 reporter's note d (2011).

209. *Id.* § 39 cmt. e, illus. 7.

210. On the timing of the City's discovery of the Association's "skipping," see *infra* note 232 and accompanying text (finding that the Association's performance was monitored throughout the contract term).

211. RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39 cmt. d, illus. 7 (2011).

212. *City of New Orleans v. Firemen's Charitable Assoc.*, 9 So. 486, 488 (La. 1891).

213. *Id.* at 486–87.

found satisfactory by the plaintiff.<sup>214</sup> Indeed, the plaintiff seems to have failed even to argue a breach of the obligations which were identified to the contract: "There is no averment in the petition that the fires were not extinguished as required by the contract, or that the fire department, under the control and management of the defendant association, was not efficient."<sup>215</sup>

The reason this matters for our purposes is that it puts a different light on what Kull is driving at when he says that "the contract price is negotiated as a function thereof."<sup>216</sup> In Kull's example, and in the reading of *City of New Orleans* in the Birksian argument, this means that a price was negotiated which reflected the literal provision of the men and equipment in the City's list, on which the Association then "skimped." Though the report is not as clear as one would wish, in my opinion this will not have happened in the actual case, where we find that, perhaps unsurprisingly given what we know of the case, the "Association was the lowest bidder."<sup>217</sup> In sum, in the actual case, if not in the illustration, the City obtained a perfectly satisfactory performance at the lowest price, and surely this shows the case is right, and reversing it would defeat freedom of contract, for the negotiations proceeded on a compensatory basis, which disgorgement based on restitution would entirely upset.

"Illustration 7," Kull tells us

[m]ight be directly explained, within the terms of § 39, as a case in which the parties' bargain would be inherently insecure if its enforcement were limited to damages for breach. (Such a rule invites the promisor to speculate by bargaining for one performance and rendering another, calculating that its saved expenditure will exceed the measurable difference in end result. This form of speculation—however well-informed or 'efficient'—exposes the promisee to unquantifiable risks against which the promisee had attempted to protect itself by contract).<sup>218</sup>

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214. See *infra* text accompanying note 233 (noting that the Association's performance was monitored and a bond was paid).

215. *City of New Orleans*, 9 So. at 488. One can, of course, imagine an argument for the plaintiff, such as that the amount of resource employed by the defendant was a source of insecurity which was a breach, but no such argument was made, and it would, one imagines, have run into serious certainty problems even if liability were established.

216. RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39 cmt. d, illus. 7 (2011).

217. *City of New Orleans*, 9 So. at 487.

218. RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39 cmt. e (Tentative Draft No. 4, 2005).

With respect, this is not the source of the problem in Illustration 7, much less in *City of New Orleans* itself, for there is nothing in the law which mandates that "enforcement" be "limited to damages for breach." In the Illustration, the City wants literal provision of the men and equipment. Were it competent in its negotiations, it should have realized that compensatory damages were not going to do the necessary work, for deficiency in the literal provision would not, of itself, cause a loss, and the City should have negotiated for something it would have found better.

From the point of view of "justice," viewed not only after the event but when, surely unusually, all the facts are thought to have come to hand,<sup>219</sup> one might be able to argue that there is a deficiency in the remedy available to the plaintiff set out in this illustration. But contracts are not made *sub specie aeternitatis*. They are made in situations in which the existence of positive transaction costs leads to bounded rationality and the negotiations by which one seeks what one wants from the contract never give perfect assurance that one will get it, much less that the contract will be "just" (whatever that means). If one does not get what one wanted out of a freely negotiated contract, one has to put up with this unless one can show a breach (which also involves transaction costs). Part of one's competence as a commercial party is competence to negotiate in such a way that this will happen. This, not entirely obscure, doctrine is called freedom of contract. One can barely imagine the haste with which Lord Woolf, who placed such reliance on *City of New Orleans* in *Blake*, would himself have denied that the plaintiff had a cause of action were the plaintiff to have denied the existence of the contract at all because the defendant had furnished inadequate consideration,<sup>220</sup> and that the contract therefore was unfair. Of course, had the City negotiated so that it became plain that a remedy would be sought which would (assuming it was possible) have secured the literal provision of the listed men and equipment, the price would have been different, and the better than compensatory remedy stipulated far more likely to be awarded after breach. But this would have been a different contract. In *City of New Orleans* itself, where the literal provision of the men and equipment was not even identified to the contract, the disregard of freedom of contract by giving the restitutionary remedy would be

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219. See *infra* text accompanying notes 230–32 (noting the City's continual monitoring of the Association's performance).

220. This is more, but by no means entirely, clearly understood in the most instructive English case on "skimping." *White Arrow Express Ltd. & Ors v. Lamey's Distribution Ltd.*, [1995] C.L.C. 1251.

indefensible. It is important for us to understand why the restitutionary perspective leads one towards such disregard.

The basic argument of this Article has been that even in the simple sale which is the paradigm, discrete contract is based on cooperation, and that widely available restitutionary remedies would undermine this. In his generous personal comments on this Article, Kull has argued that *Wrotham Park* is not a case that exhibited much cooperation, and were this the case, it would, of course, pose a serious problem for my argument, particularly as it is based on the relational theory, for that theory is generally interpreted as a very paternalistic theory,<sup>221</sup> suspicious of freedom of contract and having no or little place for competition.<sup>222</sup> But, as I have argued elsewhere, this certainly was not Ian Macneil's intention,<sup>223</sup> and, drawing on his work, the relational theory can readily be restated in such a way as to give competition a central place in it.<sup>224</sup> In my opinion, a principal virtue of the relational theory is the way that it can consistently locate legitimate competition within a framework of contract (and other) law, thereby avoiding the shortcomings of the purportedly purely individualistic view of economic action common to the (neo)classical law of contract and mainstream economics, exemplified in legal scholarship in Posnerian law

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221. Kennedy's rightly very influential gloss on particularly the work of Macaulay seems to have played a large part in this, though Kennedy's views are much more nuanced than the title of his paper would seem to have led many who have cited it to believe. Duncan Kennedy, *Distributive and Paternalist Motives in Contract and Tort Law, with Special Reference to Compulsory Terms and Unequal Bargaining Power*, 41 MD. L. REV. 563 (1982).

222. See Gunther Teubner, *Contracting Worlds: The Many Autonomies of Private Law*, 9 SOC. & LEGAL STUD. 399, 405 (2000) ("Relational contracting is out of step with today's realities if it is understood as the warm, human, cooperative interpersonal relation that overcomes the cold economic instrumentalism with a communitarian orientation, as market transactionalism with a human face."). See in criticism David Campbell, *The Limits of Concept Formation in Legal Science*, 9 SOC. & LEGAL STUD. 439, 445 (2000) ("Macneil has persevered discreteness and competition within a general relational theory, and has been highly critical of what he thinks is the unacceptable communitarianism of those who do not do so.").

223. See David Campbell, *Ian Macneil and the Relational Theory of Contract*, in IAN R. MACNEIL, *THE RELATIONAL THEORY OF CONTRACT* 3, 20–27 (David Campbell ed., 2001) ("[T]his account of co-operation in relational contracting makes it imperative to give a compatible account of competition, and in his developed work Macneil does so in two ways . . . based on his concepts of the discrete and the relational contract norms and of presentation.").

224. See, e.g., Campbell, *The Relational Constitution of the Discrete Contract*, *supra* note 170, at 56 ("We should recognize that *all* contracts, including the discrete contract, are relationally constituted and . . . the problem of securing optimal outcomes in *all* contract [is] *one* of choice of [the] appropriate relational constitution." (citations omitted)).

and economics. This is, perhaps, an occasion on which the value of the way competition may be described in the relational theory may be illustrated.

The relational theory posits a spectrum of orientations of contractual action,<sup>225</sup> from what we have seen Macneil call the "discrete" contract, exemplified by the simple sale, towards what is generally called the "relational," but which, to avoid an unhelpful confusion of terminology, I believe it best to call the "complex," contract,<sup>226</sup> in which the parties may have many "intertwined," long-lasting commitments. This Article has focused upon the cooperation largely unconsciously exhibited in the discrete contract. In the complex contract, there is a much more developed awareness of the necessity of cooperation between the parties.<sup>227</sup> Indeed, the existence of this awareness was a major stimulus to Macaulay's and Macneil's development of the relational theory. As the complexity of projects increases, it becomes increasingly difficult to specify contractual obligations at the time of agreement, and provision for explicit cooperation in the planning, monitoring and modification of obligations should be made.<sup>228</sup> At the complex end of the spectrum, cooperation may merge towards complete identification of the interests of the parties, with the next step, as it were, off the end of the spectrum being the abandonment of market organization and its replacement by integration, as formerly legally distinct stages of the production process are subsumed into one firm.<sup>229</sup>

How was cooperation to be established in *City of New Orleans*, which certainly involved a contract towards the complex end of the relational spectrum? As with other more complex contracts, it should have been established by conscious cooperation in negotiations which the parties undertook in the knowledge that the default rules encouraging automatic

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225. See generally Ian R. Macneil, *Values in Contract: Internal and External*, 78 *Nw. U. L. REV.* 340, 346–66 (1983).

226. Campbell, *supra* note 223, at 15–20.

227. Campbell & Harris, *supra* note 184, at 168 ("[W]hat the evidence shows . . . to be the case, is that failures under [long-term contract] circumstances lead . . . to extra-legal strategies to keep the long-term relationship alive in all but the most acute circumstances.").

228. Macneil, *supra* note 26, at 633 (discussing relational contracts as those involving "significant duration," "the object of exchange typically involving . . . quantities not easily measured," "future cooperative behavior is anticipated," and "[t]he benefits and burdens of the relation are to be shared rather than divided and allocated").

229. See Macneil, *supra* note 158, at 1025–37 (discussing how as long-term contractual relations endure, separate entities tend to merge, if not totally, at least for means of production of some discrete good). Of course, the various persons involved in the firm are by no means monolithically united in their interests, but the point is that the firm is organized through a single authority.

cooperation in the discrete contract would not work. And, indeed, this was to some, but a limited, extent the case.

In Kull's Illustration 7, it will be recalled that it was "after the [contract period had] elapsed [that the] City discovers that Association consistently devoted fewer men, horses and wagons to City's fire protection than the numbers required by the contract."<sup>230</sup> One wonders how the City made this discovery. In the ideal typical discrete contract, how one party manages its performance is of no interest to the other party, and the parties will remain in mutual ignorance about this. There must have been something unusual, or at least not discrete, about *City of New Orleans* itself for the facts about the "skimping" ever to come to hand.<sup>231</sup> The report does not allow one to be as clear as one would wish about how this happened, but, rather than the amount of resource provided being discovered at the end of the contract, as in Kull's illustration, the Association's performance would appear to have been continually monitored by "a board of commissioners . . . designated in [the] contract to see to its faithful performance."<sup>232</sup> The parties did, then, set up a monitoring structure (and an assurance of remedy in the form of a bond).<sup>233</sup>

For the purpose of understanding the decision in *City of New Orleans*, the most important point is that the monitoring does not seem to have been directed at the literal employment of the men and equipment, but at the satisfactory performance of the contract in the way described above, which was approved throughout the contract duration, "[d]uring the execution of the contract, the City accepted the fire department [sic] tendered by the Association with the alleged deficiencies."<sup>234</sup> Though the report is lacking, as I have said, facts like these explain the decision in the case. But what is most important for the general argument is the necessity of monitoring.

Though the quantification of compensatory damages may well not be the simplest of tasks, the plaintiff attempting it is enormously aided by the fact that, in the nature of the case, the loss is his, and he will be in as good a

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230. RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 39 cmt. d, illus. 7 (2011).

231. Even the very best English commentators have not paid enough attention to this. See Hugh Beale, *Exceptional Measures of Damages in Contract*, in WRONGS AND REMEDIES IN THE TWENTY-FIRST CENTURY 217, 232 (Peter Birks ed., 1996) (discussing *City of New Orleans* and stating "later it was discovered that [the Association] had not [kept the specified number of men, etc.] and had thereby saved themselves \$40,000").

232. *City of New Orleans v. Firemen's Charitable Assoc.*, 9 So. 486, 488 (La. 1891).

233. *Id.*

234. *Id.*

position as possible to assess it. Restitution for wrongs is not like this, for the plaintiff has to provide evidence of the (savings or) gains made by the defendant, who obviously will not want to provide this evidence. The civil legal system does in theory have the mechanisms for searching for and compelling disclosure of evidence in these circumstances, but this process can be extremely fraught and expensive,<sup>235</sup> involving the use of court orders which Sir John Donaldson M.R. (as he then was) memorably called "the nuclear weapons" of commercial litigation.<sup>236</sup>

In practice, certainly in England and Wales, the plaintiff's difficulties are reduced because, to be frank, the courts have often adopted a not very defensibly rough and ready approach to the quantification of what might be called disgorgement awards. The excuse given for this—that there is nothing better to be done—is correct *ex post*. But these proof problems arise in this acute form only because the parties have not addressed them *ex ante*, at the time of agreement, when a structure for avoiding them surely would be sought by a competent party contemplating a restitutionary remedy. The absence of such a structure is *prima facie* evidence that such a remedy was not identified to the contract, and therefore should not be awarded. If the courts were less prepared to be rough and ready, this would concentrate the minds of potential plaintiffs wonderfully. It is highly significant that the actual litigation in many of the English cases mentioned above, which have formed what I have called the canon of the Birksian argument, have actually been about the securing of this evidence after the event.<sup>237</sup>

Consideration of these practical issues does not naturally arise in the English restitutionary literature, on which the abstract, theoretical concerns of Peter Birks have left their mark. So concerned with abstract wrongs that, for once ignoring the wisdom to be gleaned from ancient maxim, in this case "ask a silly question, get a silly answer," the characteristic problem

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235. And oppressive from the point of view of the defendant.

236. *Bank Mellat v. Nikpour*, [1985] F.S.R. 87, 92.

237. One notable example is the first instance proceedings in *Experience Hendrix LLC v. PPX Enter. Inc., Edward Chalpin*, [2002] EWHC 1353 (QB) [48] ("Mr. Chalpin's subterfuge . . . in keeping the best and usable masters and copies . . . is unhelpful to his cause. However, on this issue I do not think that the Claimant has helped himself and is guilty of undue delay. . . . I am not moved to grant an Order for delivery up."). For a discussion of this case see *Campbell & Wylie*, *supra* note 32, at 623–25 ("An important subsidiary issue in *Hendrix* was the claimant's attempt to enlist the Court's assistance in securing the information need to obtain an account . . ."). See also the discussion of *Teacher v. Calder* in *Campbell* *supra* note 35, at 266–68 ("Talk of that [restitutionary] remedy assumed that the claimant has knowledge of the defendant's profit so that he is aware of the possibility of disgorgement. There is, of course no necessity for the claimant to have this knowledge . . .").



considered in the Birksian argument is the liability which would follow from a hypothetical householder secretly watching a hypothetical window cleaner mistakenly or speculatively clean his windows.<sup>238</sup> (One is never told why the householder who does not wish to pay voluntarily discloses the facts that raise the possibility that he might have to.) Are wrongs to be corrected only when chance leads to their discovery and guides their correction, or would the wider availability of the restitutionary remedy lead to the imposition of disclosure requirements, and a means for monitoring compliance, with the attendant growth in transaction costs? That no real attempt has been made to address these issues in the thirty-five years since *Wrotham Park* shows that the Birksian argument is much more a flight of academic fancy rather than a responsible attempt at law reform.<sup>239</sup> As I have said and am anxious to stress, Kull's and Roberts's attitude is of a quite different stamp, but the problems still remain. The solution to these problems lies in the hands of the parties, and we should try to make them conscious of this in an instance of making explicit the lessons of contract practice which is the general method of the relational theory. This solution is quite the opposite of changing the law to match the parties' current lack of self-consciousness of what they are doing when they contract, expressed in their troublesomely mistaken faith in *pacta sunt servanda*.

I believe that cases like *Wrotham Park* arise from a general mistaken belief in *pacta sunt servanda* and from the problem of uncompensated loss which, in an important sense, it causes. I do not doubt this is an important problem; indeed, I trust it is now clear that I believe that excessively literal belief in *pacta sunt servanda* is the principal problem of the practice of contracting for remedies. But I believe that, far from changing the law to try (and inevitably fail) to give effect to the mistaken belief, it is far better that the parties themselves deal with the problems so poorly dealt with in *Wrotham Park* and succeeding cases. In order to do this, parties need to understand what they are doing when they contract, and this requires them to reject their literal belief in *pacta sunt servanda*. *Wrotham Park* arose, then, from a serious problem, which it is important to try to solve. But this is not how *Blake* arose.

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238. Reaching a pinnacle of absurdity in Peter Birks, *In Defence of Free Acceptance*, in *ESSAYS ON THE LAW OF RESTITUTION* 105, 121–24 (Andrew Burrows ed., 1991).

239. See generally HEDLEY, *RESTITUTION: ITS DIVISION AND ORDERING*, *supra* note 63; Campbell, *supra* note 63.

IX. *Why Blake Arose*

The most generous construction one can put on *Blake* is that the U.K. government was so upset by Blake's conduct that, determined to make sure he could not profit from his memoirs, it ignored the good arguments against bringing this action.<sup>240</sup> Apart from what is said in *Blake* itself, there is a considerable tone of outrage at Blake's conduct in the relevant academic literature, including the contributions of Birks.<sup>241</sup> U.S. readers may recall the emotional atmosphere that surrounded *Snepp v. United States*,<sup>242</sup> a somewhat tendentious reading of which clearly informed the argument pursued in *Blake*.<sup>243</sup> Leaving aside the costs and the remote prospect of success at the start of the action, which would have deterred almost any private person from bringing it,<sup>244</sup> Hedley was to the fore of those pointing out that there are many substantial arguments against seeking the *Blake* remedy, even in *Blake* itself.<sup>245</sup> There are many books published, say by

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240. And even more persevering with it after what one must describe as a serious defeat at first instance, when the public law aspects of the case were to the fore: Attorney Gen. v. Blake, [1997] Ch. 84 (Ch.D.) 85 ("[T]he pleadings and evidence did not disclose any breach of duty owed to the Crown on which the relief claimed could be founded." (citations omitted)). Discussion of *Blake*, including, I must admit, my own, has typically passed over the finding that George Blake breached a simple contractual obligation, even though it wholly unpersuasive, in the belief that it was not worth arguing about once the case reached the House of Lords on this basis. But, the late Professor Simpson eventually did what should have been done a decade ago, and argued that *Blake* is *per incuriam* because no breach of contract was ever shown. A.W. Brian Simpson, *A Decision Per Incuriam*, 125 LAW Q. REV. 433 (2009).

241. See Peter Birks, *A Lifelong Obligation of Confidence*, 105 LAW Q. REV. 501, 502 (1989) ("It is less obvious that a treacherous agent should be beyond the law's reach in a friendly state and one which both shares the same conception of justice and offers the defector the same conditions of life.").

242. See *Snepp v. United States*, 444 U.S. 507, 515–16 (1980) (imposing a constructive trust upon the profits of an ex-CIA agent's book, which had been written without preclearance by the CIA as required by contract).

243. See Birks, *supra* note 102, at 438 (noting the use of the term "fiduciary" in *Snepp* in order to apply the constructive trust and stating that "the word 'fiduciary' urgently needs to be purged of its over-extension. . . . [T]he time is ripe for an open acceptance of the possibility of restitutionary damages for breach of contract").

244. See HARRIS ET AL., *supra* note 32, at 266–67 ("It is impossible to believe a commercial party would have risked the hazards of litigation whose success depended on a major exercise of judicial legislation.").

245. Steve Hedley, *Very Much the Wrong People*, WEB J. CURRENT LEGAL ISSUES (2000) <http://webjcli.ncl.ac.uk/2000/issue4/hedley4.html> (last visited May 20, 2011) ("In any event, was Blake's breach of contract really so serious? His treachery was, certainly. It doomed large numbers of agents to imprisonment or death, and it wasted many years' worth of work by British and other secret services.") (on file with the Washington and Lee Law

gangsters, that are similarly questionable, and there is no moral reason corrigible as law for singling out even the contemptible George Blake. The government's outrage can hardly have been felt by all those it represents, for, to the extent that *Blake* was going to make any profit, he obviously could do so only if a large number of people bought his book. And then there is the problem of having to deal with the precedent set for commercial cases by this *outré*, if not quite unique, case. Sir Richard Buxton, a former Lord Justice of Appeal, has cited *Blake* in the course of telling a cautionary tale against judicial legislation,<sup>246</sup> but, of course, Lord Hobhouse said all this in *Blake* itself.

#### X. A Most Important Point of Clarification

It is obvious that my argument is a defence of freedom of contract and the working of the market mechanism. However, in this case, as in so many others, the market mechanism needs this defence because its nature is misunderstood. It is my belief that the relational theory of contract can make an indispensable contribution to improving our understanding by providing, not only a theory of the complex contract involving conscious cooperation, but also a theory of the discrete contract and therefore of competition based on a cooperation of which we typically are not, at the moment, conscious. The questioning of the current law of remedies has gained its basic strength from its ability to depict the position in which the defendant can choose to breach if he pays the price of doing so as unacceptably amoral or immoral. At root, this is a criticism of what is mistakenly taken to be pure economic action, with the breaching defendant portrayed as committing a wrong because his economic self-interest drives

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Review). The article continues:

But that is a judgment on Blake's life, not on his manuscript or its contractual status. It is most unclear how it can be said that Blake's breach is a serious one, and it is hard to dispel the suspicion that he is being judged by quite different criteria from those openly stated. And the insistence that the Crown 'had and has a legitimate interest' in preventing Blake from making a profit seems to beg the question. Why does the Crown have an interest in preventing the publication of the book, which it agrees is neither confidential nor prejudicial to security?

*Id.*

246. See Richard Buxton, *How the Common Law Gets Made: Hedley Byrne and Other Cautionary Tales*, 125 LAW Q. REV. 60, 73–78 (2009) ("An admittedly exceptional claims for an account as a remedy for breach of contract was allowed on the basis that the conduct of the defendant was something like breach of confidence or something like breach of a fiduciary obligation.").

him to do so, in defiance of his legal, and therefore moral, obligations. But this essentially legal approach surely rests on a basic mistake. For economic action within the parameters of the common law is by no means immoral or amoral; and its value lies in the fact that it is neither.

It certainly is the case that the (neo)classical law of contract and mainstream economics display an, as it were, moral minimalism in their attitude to the role of law in the economy, and this has been emphasized in the unsavory aspects of Posnerian law and economics. But, save libertarian anarchists, all those committed to market ordering acknowledge the role of the state in channelling maximizing behaviour into productive lines to the extent of insisting that goods may legitimately be acquired only by exchange, rather than by force or fraud. The "enforcement" of contracts is central to this; indeed, sometimes it seems to be all there is to it. But, leaving aside the political philosophical objections one may make to the various conceptions of the minimal state, I hope it is now clear that any account of the enforcement of contracts as a rather simple matter, the simplicity captured (and simultaneously obscured) in the maxim *pacta sunt servanda*, is just an inadequate account of the law.

Though we have looked only at the bare essentials of the law of remedies for breach of contract, it is obvious that the *laissez faire* rhetoric of simplicity and minimalism is implausible, for even those bare essentials involve, as we have seen, numerous complex choices between alternative forms of enforcement. If we follow Coase's definition of economic regulation as "the establishment of the legal framework within which economic activity is carried out,"<sup>247</sup> then it becomes clear that a basically negative attitude towards the state's role in such regulation is far too sweeping. For though the point is to regulate *for* choice, not to regulate *for* the imposition of a pattern, the vital work of "framework setting" or "institutional direction"<sup>248</sup> necessary for choice must be approached with a positive attitude, for inevitably it is a complex matter requiring extensive, continuous regulatory effort, and recognition that what is being regulated is contract as a spectrum of cooperative relationships (within which legitimate competition may take place).

The difficulties of reconciling the other-regarding aspect of the exchange *relationship* with the explanation of economic action in terms of pure individual maximization are insuperable. We have seen that the law of

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247. Ronald H. Coase, *Advertising and Free Speech*, 6 J. LEGAL STUD. 1, 5 (1977).

248. David Campbell & Matthias Klaes, *The Principle of Institutional Direction: Coase's Regulatory Critique of Intervention*, 29 CAMBRIDGE J. ECON. 263, 265, 278 (2005).

contract establishes a fundamentally cooperative relationship between the parties within which competition about price takes place, and the optimum levels of precaution and liability, and therefore a rational price, are set. Without this cooperative relationship, rational price determination, and therefore rational utility maximization, are impossible.

In sum, analysis of the basic legal framework for the sale of goods, the paradigm case of exchange envisaged in micro-economics at all levels of sophistication, from the high theoretical to the common practical, teaches us that: (1) welfare enhancing competition must be based on an ontologically prior cooperation between the parties to particular exchanges and between economic actors in the market economy in general; and (2) the framework for such cooperation, and therefore for defensible market ordering, has to be provided by more or less complex regulation in Coase's sense.

### *XI. Conclusion*

The extension of a restitutionary remedy to breach of contract regarded as a wrong has encountered all sorts of problems in the English case law following *Blake*. A change to the law as radical as that which it was sought to effect in *Blake* is, of course, bound to throw up problems on this scale, and whether it is worth the effort of dealing with them will turn on whether the change is worthwhile. In my opinion, the change effected by *Blake* is a drastic mistake, and the problems it has thrown up have proven and will continue to prove unsolvable because that change is inconsistent with the fundamental values of the law of contract, principally economic efficiency and freedom of choice, which boil down to the same thing.

The U.S. discussion of these issues is indebted to Roberts, who, building on the excellent work of Kull, has set out the moral argument for restitutionary remedies, and its corollary legal argument in terms of modification of the law of mitigation, in a clear way. This moral issue is what is of basic importance, and she is to be congratulated for identifying it as such, at a far earlier stage of the U.S. discussion than has been achieved in the Commonwealth. Nevertheless, she is, in my opinion, fundamentally wrong. Expectation-based damages are moral, for they institutionalize the cooperative response to breach that is at the heart of the success of the law of contract. But it was possible to make so drastic a mistake about the need for restitutionary damages only because the expectation-based law of remedies invited it. The fundamentally cooperative nature of that law is obscure, and was further obscured by Posner's early discussions of efficient

breach. In this situation, it has seemed necessary to criticize the expectation-based law of remedies as undesirably immoral or amoral, and to put forward restitutionary damages to give the law of remedies appropriate moral force. This is wrong, but the stress on moral force is right. Perhaps the fundamental service Professor Kull's drafting of Section 39, and Professor Roberts's observations upon that Section, will render is making the moral nature, and the consequent value, of the existing law of remedies clear.

