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RESTITUTION FOR WRONGS

This article examines the theoretical justifications in awarding restitutionary damages for civil wrongs and argues that restitutionary damages should be available as of right so long as appropriate rules of causation and remoteness to the different kinds of wrongs are developed as well. In addition the scope of proprietary remedies should be rationalised and should only be explicable on institutional constructive trust principles. Only exceptionally should the remedial constructive trust be invoked.

THE usual response to civil wrongs is compensation for the plaintiff's loss. Restitutionary damages is distinguished from compensation because it is a response which consists of causing the defendant to give up to the plaintiff an enrichment received at his expense. This enrichment has nothing to do with the plaintiff's loss. Restitutionary damages is an interesting alternative to the traditional remedies for civil wrongs. The intuitive position is that no one should benefit from his own wrong, *ergo* all gain-based claims should be allowed when the defendant has obtained an enrichment by committing a wrong to the plaintiff, subject to any available defences. Logic suggests that if no one is permitted to profit from his wrong, this applies irrespective of the nature of the wrong. However the courts are reluctant to contemplate the possibility of novel restitutionary claims for benefits gained and do not have an uniform view as to when the normal remedy of compensation should be departed from or why the gain should be given to the plaintiff.

Recent judicial elucidations have thrown new light on the awarding of restitutionary damages in contract and a recent English Law Reform Commission has recently published a paper on non-compensatory damages, including restitutionary damages.[1] At least as much controversy is generated in the course of academic development of the law of restitution. In addition, this area is complicated by the fact that the courts are reluctant to analyse the relief awarded as restitution. Instead, the early cases on conversion and usurping of office relied on the notions of 'waiver of tort'.[2] The term 'waiver

1 Law Commission, *Aggravated, Exemplary and Restitutionary Damages*, Law Com No 247 (1997).

2 See *Lamine* v *Dorrell* (1702) 92 ER 303; *Chesworth* v *Farrar* [1967] 1 QB 407.

of tort' served a useful but limited approach to determine when restitution was appropriate. By viewing restitution as an alternative to tort damages, the courts were able to rely on developed principles of tort law to define cases. The problem was that the terminology 'waiver of tort' connoted that the tort was ratified and hence extinguished, whereas the reality was that the tort was very much the cause of action. In *United Australia* v *Barclays Bank*,[3] this fallacy was exposed. The quasi-contractual claim in assumpsit and the tort claim were held to give rise to alternative remedies and were not based on inconsistent rights.[4]

This article argues that restitutionary damages as a relief should be available as of right, but, at the same time, we need to develop coherent principles of remoteness and causation as limiting principles to the measure of damages. We have to specify the criteria for causation or a sufficient connection between the civil wrong and profit derived or asset held. This would be the best way forward. Not only would it be largely consistent with the results of the cases on breach of contract, tort, fiduciary duties and other causes of action, but there would also be reasonable consistency amongst all these breaches of duties, which are although formally distinct, are in this regard governed by the same policy considerations. The article also examines the nature of the restitutionary proprietary remedy and considers whether the remedial constructive trust should be awarded for restitution for wrongs.

I. Gain-based Remedies for Wrongs – Underlying Principles

A. *A Parasitic Claim or Independent Claim?*

First I shall set out the underlying principles behind restitutionary damages and how it fits into the law of restitution. I start with Professor Birks' approach. According to Birks' analytical structure, there is a central division between restitution for unjust enrichment by subtraction and restitution for wrongs.[5] Where restitution is a response to unjust enrichment by subtraction, the plaintiff has to establish four basic elements:

[3] [1941] AC 1.
[4] See Viscount Simon, at 18-19.
[5] Birks, *An Introduction to the Law of Restitution* (1985, rev 1989), ch 1.

(1) the defendant was enriched;

(2) the enrichment was at the plaintiff's expense;

(3) the enrichment was unjust due to one of the recognised unjust factors; and

(4) none of the defences apply.

Restitution for unjust enrichment by subtraction is a cause of action that arises independently of any wrong. In contrast, in the case of restitution for wrongs, the defendant's acquisition of an enrichment by the commission of a wrong to the plaintiff would be 'at the plaintiff's expense', and hence would justify the award of restitutionary damages to take away the defendant's gain. Restitution for wrongs is not an independent cause of action but is parasitic on the wrong. The focus then is to ask whether this particular cause of action for wrongs will trigger a right to restitution. For Birks, the justifications for restitutionary damages are threefold:[6] the first is deliberate recourse to wrongdoing as a means of profit; the second is on prophylactic grounds, *eg,* breaches of fiduciary duty; and the third is in any other case where there is sufficient justification bearing in mind that to award such damages would give the plaintiff a windfall and also would suppress economic activity without having regard to the harm done.

Goff & Jones has adopted the same approach. According to them, before restitution for wrongs is awarded, there must be a tort or an equitable wrong.[7] Once it can be shown that the tortfeasor has gained a benefit which would not have been gained but for the tort, he should be required to make restitution.[8]

It is important to distinguish the two categories of restitution, though a given set of facts may give rise to genuine alternative claims. I use the cases on the recovery of bribes pocketed by a dishonest fiduciary from third parties as an illustration. The fiduciary receives a bribe in return for procuring his principal to enter into a transaction with the briber. The bribe is paid over in ignorance of the tainted transaction. In restitutionary terms, the bribee is enriched at the principal's expense as the principal has paid more for the transaction than he had to and the principal would be able to recover the bribe as representing the difference in value of the contract.

6 Birks, "Civil Wrongs", (1990-91) *Butterworth Lectures* 1 at 94-98. *Cf* his earlier views that the tort must be an 'anti-enrichment wrong' in Birks, *ibid*, note 5, at 328.

7 Goff & Jones, *Law of Restitution* (4th ed, 1993), ch 38.

8 A limited exception was one based on policy where there are numerous plaintiffs who suffer injury or loss from the same tortious act. See Goff & Jones, *supra*, note 7, at 725.

This was what happened in *Mahesan* v *Malaysian Government Officers' Co-operative*,[9] where M, in the plaintiffs' employment, conspired with the briber that the latter should purchase a plot of land at a low price and sell it to the plaintiffs for a grossly inflated price, and M was to obtain a bribe in return. The Privy Council held that the plaintiffs could have a claim against M for the bribe or alternatively for damages for the loss sustained in consequence of entering into the transaction in which the bribe was paid. In restitutionary terms, the claim for the bribe was a cause of action in autonomous unjust enrichment. In addition, M was in breach of fiduciary duty when he accepted the bribe, and the recovery of the bribe would also fall within restitution for wrongdoing.

In contrast, the remedy awarded in *Thahir* v *Pertamina*[10] could only arise under restitution by wrongdoing. Pertamina was an Indonesian state corporation which undertook the development of an industrial complex for steel-making and related industries. General Thahir was employed by Pertamina as general assistant to the president director of Pertamina, a very senior management position. During the course of his appointment, he systematically accepted bribes from contractors. In return for the bribes, the contractors obtained better contractual terms than what they would have otherwise obtained if they had to tender for the work and received preferential treatment where payments were concerned. When General Thahir died, there were 17 separate ACU deposits denominated in deutschemarks and two deposits in US dollars in the names of General Thahir and his wife. The claim by Pertamina for a constructive trust over the ACU deposits did not fall within unjust enrichment by subtraction simply because the enrichment of the corrupt briber was not subtracted from the state corporation's wealth. In *AG of Hong Kong* v *Reid*,[11] the dishonest Acting Director of Prosecution accepted bribes in return for obstructing the prosecution of certain criminals. It is impossible to fit these two cases within autonomous unjust enrichment as the bribe originated from third party bribers, and not the principal.

B. *User of Property*

Birks' theory is not uncontroversial. Beatson,[12] the chief proponent of the independent claim theory, argues that the cases of wrongful use or misappropriation of property are in fact independent restitutionary claims as

[9] [1979] AC 374.
[10] [1994] 3 SLR 257.
[11] [1994] 1 AC 324.
[12] Beatson, 'The Nature of Waiver of Tort' in *The Use and Abuse of Unjust Enrichment* (1991), at 206.

they are based on wrongful subtraction of rights belonging the plaintiff. What is subtracted from the plaintiff is the right to have an exclusive enjoyment of the use of the property. The wrongful use of the property generates not only receipt of the benefit but also the unjust factor in satisfying the 'at the expense of' element for autonomous unjust enrichment. McGregor, along similar lines, argues that the key remains the benefit to the defendant, and the wrongdoing is only incidental and serves to show that the defendant's enrichment is unjust, but it does not make the claim dependent or parasitic.[13]

The law has always afforded stronger protection to property rights than personal rights. The nature of the proprietary right is that it is an exclusive right to property and it is not surprising to find that restitutionary damages is justified on the sole ground of misuse of the plaintiff's property. In *Halifax Building Society* v *Thomas*,[14] the mortgagor obtained the mortgage by deliberately misrepresenting his creditworthiness and identity, thereby committing the tort of deceit. The mortgagee sued unsuccessfully for his restitutionary claim for the surplus of the proceeds from the sale of the property after the mortgage was discharged. The Court of Appeal held that the mortgagee had elected to affirm the transaction and in any event, the mortgagor's enrichment was not at the mortgagee's expense. Peter Gibson LJ said that, outside the breach of fiduciary duty cases, no case showed that a wrongdoer was accountable for the profits other than through the wrongful user of the plaintiff's property. Similarly, Steyn LJ in *Surrey County Council* v *Bredero Homes*,[15] held that restitutionary awards are given only where the contractual right has achieved a proprietary status.

This notion of wrongful use of property may explain some of the cases on conversion (*Lamine* v *Dorrell* and *Chesworth* v *Farrar*) and trespass to land (*Edwards* v *Lee's Administrators*,[16] *Penarth Dock Engineering* v *Pounds*[17] and *Ministry of Defence* v *Ashman*).[18] *Phillips* v *Homfrays*[19] is regarded as a somewhat anomalous case standing in the way of restitution for tort. The deceased trespassed on the plaintiff's land by drawing coal from his land and using his underground passages to transport the coal. In the earlier action, the plaintiff was granted damages to be assessed for the coal that was mined and the use of the land against the tortfeasor. When

[13] McGregor, 'Restitutionary Damages' in Birks, *Wrongs and Remedies in the Twenty-First Century* (1996), at 203.
[14] 1996] 2 WLR 63.
[15] [1993] 1 WLR 1361.
[16] (1936) 96 SW 2d 1028.
[17] [1963] 1 Lloyd's Rep 359.
[18] [1993] 2 EGLR 102.
[19] (1883) 24 Ch D 439.

the defendant died, the Court of Appeal held that the old *actio personalis* rule operated such that the action for the use of the land did not survive. The court only allowed claims relating to the proceeds of the deceased's coal and not the trespass. The majority of the Court of Appeal held that the deceased was not enriched since he obtained only a negative benefit by saving himself of paying for the use of the wayleaves. The decision is criticised for not recognising that the saving of an expense can be a benefit.[20] However it did recognise that an action was maintainable in respect of the value of the coal taken.

However the *Halifax* formulation of user of property is neither justified conceptually nor consistent with case law. Property rights are thought to involve exclusive rights to exploit an asset in the manner sanctioned by the rights. But the very reason for the connotation of exclusivity of legal right depends on the very existence of restitutionary remedy for unlawful acts and omissions adverse to the holder of the property right, making the argument circular.[21] There are three other arguments against using the notion of user of property.

First, even if the right infringed is a proprietary right, restitutionary damages does not necessarily follow. *Stoke-on-Trent County Council* v *W & J Wass*[22] concerned an infringement of the plaintiff's proprietary right to hold a retail market and the right to stop others holding a market. Yet the plaintiff only recovered nominal damages because it could not prove its loss. The court distinguished the trespass cases in *Strand Electric & Engineering* v *Brisford Entertainments*[23] and *Penarth Dock* on the tenuous ground that in trespass the defendant's use of the plaintiff's land deprived him of any opportunity of using it himself. An unlawful use of the plaintiff's right to hold his own market did not deprive him of the opportunity of holding one himself. This aspect of the decision ignores the fact that the plaintiff had the right to stop others from holding a market and he was deprived of that right; hence there was actual interference with the plaintiff council's exclusive enjoyment of the right.

Second, what amounts to 'property' in the context of wrongful user is debatable. Is information a species of property? This is especially important in addressing the problem with a fiduciary utilising opportunities for his

[20] *Supra*, note 7, at 719.

[21] See Nolan, "Remedies for Breach of Contract: Specific Enforcement and Restitution" in *Failure of Contracts: Contractual, Restitutionary and Proprietary Consequences* (Rose ed, 1997), 35 at 40; Smith L "Disgorgement of the Profits of Breach of Contract: Property, Contract and Efficient Breach" (1994) 24 Can Bus LJ 121.

[22] [1988] 3 All ER 394.

[23] [1952] 2 QB 246.

own benefit. According to Beatson,[24] information is treated as property and the use of information gives rise to tracing. Judicial opinions conflict but the majority view is that it is not property. In *Boardman* v *Phipps*,[25] Lords Hodson and Guest accepted that information was a species of property which could properly be regarded as trust property since the only basis on which the defendants obtained their information was the fact that they had been purporting to represent the trust. The fiduciary's misuse of that trust property rendered him liable to account for all profits made as a result of that breach. Lords Cohen and Upjohn refused to accept that information was a species of property. However the majority (Lords Hodson, Guest and Cohen) agreed that the information was obtained while the defendants were purporting to represent the trust. The defendants were exploiting an opportunity for their own benefit and had placed themselves in a position of conflict of interest. In *Snepp* v *United States*,[26] information acquired by the CIA agent was held to be a species of property, and he held the profits made by him in publishing the confidential information on constructive trust. It is submitted that the better view is that information is not property that can be traced into the hands of any recipient. Otherwise the result is very inconvenient as information can be divulged in its entirety. In fiduciary cases, liability to account should only be imposed where the fiduciary places himself in a conflict of interest in using the information for his benefit. Even though confidential information has characteristics of property, to hold that it is property does not assist in resolving the issue of when a confidant or a third party who receives confidential information may be liable for misuse of confidential information.

Friedmann is an extreme proponent of the proprietary notion of the wrong and argues that appropriation of proprietary and quasi-proprietary interests should be subject to restitutionary interests. Quasi-proprietary rights are interests which do not confer exclusive rights but are protected against certain types of interference, *eg*, the right to privacy and contractual rights.[27] Similarly, Jackman argues that restitution exists to protect 'facilitative institutions', which are power-conferring facilities for the creation of private arrangements between individuals, *eg*, contract, trusts and private property, though it excludes bodily integrity or reputation (which are natural assets that exist irrespective of rights given by law.[28] The obvious drawback to these approaches

[24] *Supra*, note 12.
[25] [1967] 2 AC 46.
[26] (1980) S Ct 763.
[27] Friedmann, "Restitution of Benefits Obtained through the Appropriation of Property or the Commission of a Wrong" (1980) 80 Col LR 504.
[28] Jackman, "Restitution for Wrongs" (1989) 48 CLJ 302.

is the inherent circularity. The reasoning appears to be based on whether the restitutionary claim should be allowed before deciding whether it constitutes a property or quasi-property interest or whether it is to protect facilitative institutions.

Third, the notion of proprietary interest does not fit easily in contract and other non-proprietary interests. In the case of contract, in *Wrotham Park* v *Parkside Homes*,[29] a developer acquired land subject to a restrictive covenant for the benefit of the adjoining estate. In breach of the covenant, the developer built houses on the land. This did not diminish the value of the estate but the owners obtained damages for the breach, amounting to five per cent of the profit, as representing the "sum of money as might reasonably have been demanded by the plaintiffs from the defendants as *quid pro quo* for releasing the covenant."[30] A different result was reached in *Surrey CC* v *Bredero* where a developer bought land from the local authorities under a contract limiting the number of houses to be built. In breach of contract, the developer built more houses than stipulated under the contract and the local authorities only received nominal damages. Steyn LJ in *Surrey CC* v *Bredero* held that restitutionary awards are given only where the contract has achieved a proprietary status by virtue of the doctrine of restrictive covenant. *Wrotham Park* was explained on that basis.

C. *Re-analysis as Compensation* v *True Compensation*

In a different way, case-law has analysed many of these cases on compensatory grounds. However the loss is not calculated by reference to the position which the plaintiff would have been in if the wrong had not been committed, but instead, by reference to the position the defendant would have been in if he had taken a licence to do what he actually did without a licence. *Wrotham Park* is now explained on compensatory grounds in *Jaggard* v *Sawyer*,[31] *viz* a percentage of the profits of the defendant was taken away not to strip the defendants of their unjust gains but as compensation; there was a relationship between the profits earned by the defendants and what the defendants could reasonably have accepted as the price to secure the release from the contract.

This reasoning is hard to reconcile with *Stoke-on-Trent* where it could be argued that what the defendants ought to pay was the price for the licence that would have been granted if they had negotiated with the council,

[29] [1974] 1 WLR 798.
[30] *Ibid*, at 815.
[31] [1995] 1 WLR 269.

measured by reference to the profits earned. Jones suggests that where the defendant violates the plaintiff's proprietary rights, it should be irrelevant to ask why the defendant has failed to carry out his promise; the defendants could not complain in *Wrotham Park* because their conduct prevented the possibility of any bargain to be reached.[32] Surely the loss of opportunity is artificial in *Wrotham Park* where the owner would not have allowed the buildings to be built in breach of restrictive covenant. Millet LJ in *Jaggard* v *Sawyer* attempted to resolve this difficulty by saying that the defendant had lost the valuable right to refuse consent or to seek an injunction.[33]

The reluctance to say that restitutionary damages were awarded is also seen in trespass or user of land cases, *eg, Strand Electric* and *Penarth Dock.* In *Ministry of Defence* v *Ashman,* the wife of a member of the armed forces remained in possession of the quarters owned by the Ministry of Defence, despite being given a notice to quit, as she had no where to go. The rent which members paid was much lower than the rent which the quarters would have fetched in the open market. Lloyd LJ analysed it as one of compensatory damages, which he held was a claim for mesne profits, relying on *Penarth Dock*, though the other two judges preferred a restitutionary analysis. Kennedy LJ held that the defendant was liable for the value she would have to pay for suitable local authority accommodation had any been available, rather than the market rate. Hoffmann LJ analysed it as one of restitution, and the benefit was valued as the ordinary market value but subject to subjective devaluation which applied because of the special circumstances. In effect, what the defendant had to pay over was the amount of expense that she had saved.[34]

II. Restitutionary Damages for Breach of Contract – A Re-think

Until recently, the position was that in *Surrey CC* v *Bredero* and in *Tito* v *Waddell (No 2)*[35] *viz* restitutionary damages are not recoverable for breach of contract, unless it also infringes a proprietary right. In *Tito*, Pacific Phosphate company contracted with the landowners of Ocean Island to

[32] See Jones, "The Recovery of Benefits Gained from Breach of Contract" (1983) 99 LQR 443.

[33] *Supra*, note 31, at 210.

[34] Lloyd LJ in *Inverugie Investments* v *Hackett* [1995] 1 WLR 713 again held that any such award was one of compensation. See also Coote, 'Trespass, Mesne Profits & Restitution' (1994) 110 LQR 420, who argues that Hoffmann and Kennedy LJJ were wrong in equating the expense saved as the benefit received by the defendant.

[35] [1977] Ch 106.

replant the land once the former extracted phosphate from the island. Pacific Phosphate company, in breach of contract did not do so. The landowners could not claim the cost of replanting as compensation as they had resettled elsewhere and were unlikely to use the money so recovered to replant. Meggary J refused to require the defendants to disgorge what they had saved by not doing the work.

It is a real problem in commercial contracts where the breach of contract leads to a loss which is not quantifiable. For instance, in *Ruxley Electronics* v *Forsyth*,[36] the house-owner contracted for a swimming pool to be constructed next to his house, and specified that the pool was to be 7 feet and 6 inches at the deep end. The contractors however built a pool which had only 6 feet and 9 inches at the maximum depth. The aggrieved house-owner sued the contractors, claiming the cost of cure for reconstructing the pool, which came up to £21,650, since that was the only way to remedy the defect in depth. The non-conforming pool did not in any way diminish the value of the land on which the pool stood. Judge Diamond QC found that he was not satisfied that the owner intended to build the new pool and the cost of rebuilding was wholly disproportionate to the disadvantage of having the non-conforming pool. Instead he awarded damages only for loss of amenity, which came up to £2500. The Court of Appeal disagreed but the House of Lords eventually affirmed his decision.

Ruxley Electronics illustrates the difficulties where the breach by the contracting party has not caused a loss to the other party and whose expectation is not quantifiable by market value. The House of Lords found that it was unreasonable for the owner to insist on reinstatement where the expense of the work involved was out of proportion to the benefit to be obtained. Yet the Law Lords did not accept that the difference in market value was the only other alternative (which would yield only nominal damages). The owner did lose his preference as to the depth of the pool of his specification, and hence was awarded damages for loss of amenity. Lord Mustill stressed that it would be unacceptable if the contractors were allowed to keep the contract price, calculated to reflect the obligations they were undertaking, without being required to comply with those obligations, where the only reason was that the other party's expectation was not reflected in the market value of performance. In *Ruxley Electronics*, no argument was raised as to whether the owner could recover from the contractors any savings in the money.

[36] [1996] 1 AC 344.

In construction contracts, there is a persistent risk of under-compensation.[37] Unlike other cases, such breaches would leave the plaintiff with a performance he could not reject, retain or dispose of by way of mitigation in order to fulfil his expectation, other than by the unrealistic means of selling the property comprising the defect and purchasing another. Cost of cure is not always available and estimates of consumer surplus are likely to be unpredictable. Yet there is the need to protect the plaintiff's legitimate interest in having the contract performed. One method is to hold that there is a general right to recover gains flowing from a breach of contract unless the plaintiff's expectations are fully protected by a compensatory award. The counter-argument is that we ought to address the inadequacy of compensation remedies since restitution only aids the plaintiffs whose defendants make profits.

An important development is the recent English Court of Appeal decision in *Attorney-General* v *Blake*.[38] Blake, a former secret service agent convicted of being a spy, published an autobiography, in breach of contract with the government, disclosing information about the service without prior notice. The Attorney-General brought an action against Blake for damages for breach of fiduciary duty and payment of all moneys received or to be received. The Court of Appeal held that the Crown could not establish loss and was hence only entitled to nominal damages. The Attorney-General did not advance the arguments on a private law claim to restitutionary damages for breach of contract but relied on its alternative claim in public law based on Blake's breach of the Official Secrets Act. Nevertheless, the Court of Appeal went on to express its view on restitutionary damages. Lord Woolf MR held that the "law is now sufficiently mature to recognise a restitutionary claim for profits made from a breach of contract in appropriate circumstances".[39] His Lordship held that if the court was unable to award restitutionary damages for breach of contract, the law of contract would be seriously defective; because the law failed to attach a value to the plaintiff's legitimate interest in having the contract duly performed. The basis on which damages were awarded should not depend on the defendant's moral culpability and it was not enough to show that the defendant had breached the contract in order to perform a more profitable contract. Instead there were two situations where justice required the award of restitutionary damages:

[37] See O'Sullivan, "Loss and Gain at Greater Depth: The Implications of *Ruxley* decision" in *Failure of Contracts: Contractual, Restitutionary and Proprietary Consequences, supra*, note 21, at 1.

[38] [1998] 1 All ER 833.

[39] *Ibid*, at 845.

(1) skimped performance (*ie,* where the defendant had failed to provide the full extent of services he had contracted to provide and has charged the plaintiff); and

(2) where a defendant had obtained his profit by doing the very thing he had contracted not to do. On the facts, Blake had promised not to disclose official information and yet he had done so for profit. Consequently he would be liable for restitutionary damages.

It remains to be seen how the concepts of skimped performance and the defendant's obtaining the very thing he contracted not to do will be applied in the courts. For skimped performance, there is noticeable judicial unease over the result in cases such as *City of New Orleans* v *Firemen's Charitable Association*[40] and *Tito* v *Waddell*. In *City of New Orleans*, the defendants contracted with the plaintiff to provide a fire-fighting service. Under the contract they were supposed to keep available a number of men, horses and pipes. It was later discovered that the defendants under-provided the number of men, horses and pipes and had saved over $40,000, a sizable amount. The plaintiff could not show that it had suffered any loss in being unable to fight fires during that period. The Supreme Court held that the plaintiff could not recover as it had not suffered any losses.

However, it is not immediately self-evident what the limits of disgorgement are for the second situation stated in *Blake*. In all cases, there is already an implied or express term of the contract restraining the defendant from doing what he did. If the bar against the defendant obtaining the profit in doing the "very thing he contracted not to do" is to have any meaning, he must have breached a term so important that it forms the basis of the contract. Does it bring into play the concepts of conditions, innominate terms, and warranties that are used to determine if the breach is sufficiently serious to justify termination of the contract? I suggest not. It is submitted that what Lord Woolf MR was referring to is whether, as a matter of construction of the terms of the contract, it is the intention of the parties that the defendant would be prevented from pursuing a particular profit-making activity. If so, disgorgement will be ordered. Clear cases would include employment agreements with a convenant not to disclose trade secrets to rival competitors.

In *Surrey CC*, Steyn LJ alluded to the concern that restitutionary damages do discourage economic activity and that such liability would ultimately fall on the underwriters who have incurred relevant liability risks. Subscribers to the efficient breach theory would say that the law should not deter a

[40] (1891) 9 So 486.

contracting party from committing a breach which brings him a benefit in excess of the loss for the other contracting party from that breach because the breach will be economically inefficient. The flaw of the theory is that transaction costs are not included in the analysis; where a potential contract-breaker has to negotiate for his release from his contractual obligation, the transaction costs can exceed the potential profit.[41] In addition, it ignores the fact that the promisee would often prefer the performance of the promise.

III. Equitable Wrongs

The principles underlying availability for disgorgement of profits for breach of fiduciary duty is entirely prophylactic. In the case of breach of fiduciary duty to the trustee/fiduciary to the principal/beneficiary, whether by misusing trust property or by placing himself in a position which potentially or actually conflicts with his duty to the beneficiary, it is clear that the fiduciary is personally liable to account for any profits made in breach of his duty: *Boardman* v *Phipps*.[42] The rule is strict and applies even where the fiduciary is innocent (as in *Boardman* v *Phipps*) and even where the beneficiary would not otherwise have been able to take advantage of the opportunity to make the profit for himself (*Regal Hastings* v *Gulliver*;[43] *Industrial Development Consultants* v *Cooley*).[44]

In *Boardman* v *Phipps*, the trust solicitor and one of the beneficiaries under the trust represented the trust at the meeting of a company of which the trust was a minority shareholder. During the meeting, they obtained information which would not been available to the general public and suggested to the trustees that they acquire a majority shareholding in the company. This was rejected and the trustees used the information and made a profit by acquiring a majority shareholding of the company themselves, which proved to be highly beneficial to the trust. It was held that they had placed themselves in a fiduciary relationship out of which they had obtained an opportunity to make a profit. The majority of the House of Lords held that the defendants had placed themselves in a position where their duty and interest might conflict, and were liable to account to the trust for the profits even though both of them acted honestly and openly and in a manner beneficial to the trust.

[41] See Posner, *Economic Analysis of Law* (2nd ed, 1977), at 89; Smith L, "Disgorgement of the Profits of Breach of Contract: Property, Contract and 'Efficient Breach" (1994-95) 24 CBLJ 121.

[42] [1967] 2 AC 46.

[43] [1942] 1 All ER 378.

[44] [1972] 1 WLR 443.

A different position is taken in respect of breach of confidence. The distinction turns on whether the breach is deliberate. In *Peter Pan Manufacturing* v *Corsets Silhouette,*[45] *AG* v *Guardian Newspaper*[46] and *My Kinda Town* v *Soll*,[47] an account of profits was available for breach of confidence. In *Seager* v *Copydex (No 2)*,[48] compensation was ordered for breach of confidence. *Peter Pan Manufacturing* was distinguished on the ground that *Seager* was not a case of deliberate passing-off and hence only compensatory damages were awarded. The rationale is similarly that of deterrence; in *AG* v *Guardian*, Lord Keith held that the availability of account of profits serves a useful purpose of lessening the temptation for recipients of confidential information to misuse it for financial gain.

IV. Limitations to Restitutionary Damages

A. *Measure of Restitution – Remoteness, Causation or Counter-Restitution*

In advocating a more liberal approach to restitutionary damages, limitations have to be put in place concurrently. For subtractive unjust enrichment, there are already internal restrictions since the plaintiff always has to show that the enrichment is subtracted from him. However in the case of wrongdoing, the wrongdoer can receive gains from third parties which qualify as enrichment. It may even be said that such enrichment is at the plaintiff's expense if it has been obtained as a consequence of the wrong. The danger is that the remedy becomes disproportionate to the cause of action to which the remedy is based. In this context, we are not concerned about tracing at all, but the extent to which the defendant should be personally liable at law and in equity. Remoteness and causation are used to limit recovery of damages but they are not well developed concepts in the context of restitutionary damages for wrongs.[49]

1. *Equitable Wrongs*

In equity, the courts take a strict view of breaches of fiduciary duty. The reason for the imposition of a strict duty to account where the fiduciary has breached his fiduciary duty is often said to be prophylactic, *ie,* one

[45] [1964] 1 WLR 96.
[46] [1990] 1 AC 109.
[47] [1983] RPC 407.
[48] [1964] 1 WLR 96.
[49] Birks, *supra*, note 5, at 380.

of deterring the fiduciary from the temptation of putting himself in a conflict of interest. The strict duty is only mitigated by an order of the court to make an allowance for the trustee's skill and work done, and this is only done in cases where the fiduciary has acted honestly (as in *Boardman* v *Phipps*).

It follows from the strict prophylactic stance taken by fiduciary law that certain presumptions of the rules of remoteness and causation are offered when seeking to make out a restitutionary claim. The concern is whether the fiduciary has made unauthorised profits from the trust or whether he is placed in a position of conflict of interest between his own and the beneficiary's interest. Once he is so placed, he is *prima facie* liable to account and it is irrelevant that the beneficiary may not utilise the opportunity or make the profit.

Given the advantages of relying on such presumptions of remoteness and causation in fiduciary law, there is always a temptation to fit in many commercial relationships into fiduciary law. A whole body of case-law and academic writings[50] has developed as to who is a fiduciary. In Australia, the High Court uses reliance on the defendant as a touchstone of fiduciary duty: *Hospital Products US Surgical Corporation*[51] and *United Dominions Corporation* v *Brian*.[52] In *re Goldcorp Exchange Ltd (in receivership)*,[53] the Privy Council rejected reliance as a concept since many commercial relations are based on reliance and to introduce fiduciary obligations would have adverse consequences. In *Henderson* v *Merrett*,[54] Lord Browne-Wilkinson said that the phrase "fiduciary duties" gave rise to the mistaken assumption that all fiduciaries are the given the same duties in all circumstances.[55] In a later case, *Target Holdings*,[56] he again cautioned that it was inappropriate to lift wholesale the detailed rules developed in relation to traditional trusts and apply them to trusts of a very different kind. It is submitted that we have to guard against focusing on the labels of "fiduciary" but instead to concentrate on the exact content of the relationship. The policy objectives to be achieved and the purpose of imposing the rule have to be examined carefully.

50 *Eg*, Glover, *Commercial Equity: Fiduciary Relationships* (1995), ch 2; Oakley, *Constructive Trusts* (3rd ed, 1997), at ch 3.
51 (1984) 156 CLR 41 (Gibbs J).
52 (1985) 157 CLR 1 (Mason CJ)
53 [1995] 1 AC 74.
54 [1995] 2 AC 145.
55 *Ibid*, at 206.
56 [1996] 1 AC 421 at 435.

In Australia, there is a gradual liberalisation of remedies for breach of fiduciary duty. This is aptly illustrated in the Australian High Court decision in *Warman* v *Dwyer*.[57] In *Warman* v *Dwyer*, the defendant was the general manager of the plaintiff. He conducted secret negotiations with B who was then in a distribution agreement with the plaintiff. The defendant arranged for two companies to be incorporated and B terminated the agreement with the plaintiff and entered into a joint venture agreement with the two companies and the defendant. By then the defendant had resigned from the plaintiff's employment. The plaintiff sought an account of profits made by the defendant or compensation actually sustained due to the breaches of fiduciary duty. The High Court of Australia held that the fiduciary was liable to account. The difficulty was the extent of the account of profits. It drew a distinction between the case where a specific asset is acquired and the case where a business is acquired and operated. In the case of the former, it was appropriate to order an account of all the profits generated by the use of the asset but not in the case of the latter:[58]

> In the case of the business, it may be inappropriate and inequitable to compel the errant fiduciary to account for the whole of the profit of his conduct of business or his exploitation of the principal's goodwill over an indefinite period of time. In such a case, it may be appropriate to allow the fiduciary a proportion of the profits, depending upon the particular circumstances. That may well be the case when it appears that a significant proportion of an increase in profits has been generated by the skill, efforts, property and resources of the fiduciary, the capital which he has introduced and the risks he has taken, so long as they are not risks to which the principal's property has been exposed. Then it may be said that the relevant proportion of the increased profits is not the product or consequence of the plaintiffs' property but the product of the fiduciary's skill, efforts, property and resources. That is not to say that the liability of a fiduciary to account should be governed by the doctrine of unjust enrichment, though that doctrine may well have a useful part to play; it is simply to say that the stringent rule requiring a fiduciary to account for profits can be carried to extremes and in cases outside the realm of specific assets, the liability of the fiduciary should not be transformed into a verdict for the unjust enrichment of the plaintiff.

[57] (1995) 182 CLR 544.
[58] *Ibid*, at 561.

The High Court held that there has to be a direct attribution of the profits to the breach, not a but-for test of causal connection between the breach of fiduciary duty and the benefit to the fiduciary. It refused to take the blanket view that once a fiduciary relationship was established, the plaintiff could establish an account even if the principal could not utilise the profit. The prophylactic rationale behind fiduciary law has far less force in a commercial context, especially where the skills of the defendant are necessary. The defendant does not immediately make profits by expropriating the opportunity of entering into the joint venture for his own benefit. His own efforts and skills are also required to turn the joint venture into profit-making. The plaintiff lost the distributorship agreement which would have survived only for a further year. The defendant should account for his profits which arose from his involvement in the two companies but only for a period of two years. An allowance was made for expenses, skill, expertise and resources by the defendant.

2. *Contract*

In the case of contract, once we apply a more stringent test of causation and remoteness, we would find that the result would be consistent with the general denial of restitutionary damages for breach of contract. However it is submitted that it is not because contract law should be exempted from disgorgement, but the manner in which the rules of remoteness and causation are applied. I have shown that in *Warman*, the skills of the defendant were required before the joint venture turned out to be profit-making; mere expropriation of the business opportunity does not. Similarly, for breach of restrictive covenant in employment contracts not involving fiduciary duties and, in the local context, breach of scholarship agreements, the employer or the scholarship provider should not be able to recover the salary which the defendant earned with a different employer.[59] None of the generous presumptions in fiduciary law applies. The plaintiff has to show that the profit made by the defendant was attributed to the breach of contract. Where the profits require skill and initiative on the part of the defendant, as in most cases, the plaintiff will not be able to show that the profits were made entirely in consequence of the breach of contract.

In the case of skimped performance or saved expenses as envisaged in *Blake*, it really does not lie in the mouth of the defendant to argue that the expenses saved were not the direct consequence of the breach of contract

[59] *Cf* Jones, "The Recovery of Benefits Gained from Breach of Contract," *supra*, note 32, at 456.

with the plaintiff. If the terms of the contract were duly performed, such expenses would not have been saved and the plaintiff was entitled to claim these expenses.

Another example would be a contract for the purchase of generic goods. If the seller was able to find a second buyer willing to pay a higher price and thus refused to sell the goods to the first buyer, the first buyer would not be able to claim the profits made by the seller from breaching the contract. He could have gone to the market and obtained the substitute goods.

3. *Counter-restitution*

The allowance for expenses, skill and expertise has been justified on the principle of counter-restitution,[60] which is that the plaintiff wishing to reverse unjust enrichment which the defendant has obtained at his expense must recompense the defendant for any benefit which he has received at the defendant's expense. However, it is uncertain if such a defence is available as of right to any wrongdoer. In *Boardman* v *Phipps*, the trustees were held accountable for the profits made in breach of trust but an allowance was awarded for the work done. Lords Cohen and Hodson took the view that the allowance should be a liberal one. In *Guinness* v *Saunders*,[61] where the allowance was not made on the ground that the defendant director had deliberately placed himself in a conflict of interest by tying his remuneration to a percentage of the amount paid by his principal in respect of the take-over, Lord Goff said that the allowance for work and skill could only be allowed where the exercise of the equitable jurisdiction did not conflict with the policy underlying the rule. To allow the claim by the director would be to encourage trustees to put themselves in a position where their interests conflicted with their duties as trustees.

It is submitted that, ultimately, it is a matter of degree and a matter of discretion of the court. A trustee who puts himself in a technical conflict of interest is viewed more generously than a director advising the company on a take-over, who pegs his remuneration to the amount which the company is prepared to pay on the take-over. In the case of contract, an analogy with *Boardman* is most inappropriate since most contractual rights are clearly laid down (unlike the wide and onerous fiduciary duties) and it is most unlikely that the contract breaker thought he was entitled to do what he

[60] *Eg*, Mckendrick, "Total Failure of Consideration and Counter-restitution: Two Issues or One?" in *Laundering and Tracing* (Birks ed, 1995), ch 8, at 239.

[61] [1990] 2 AC 663.

had done. However, given that it is a matter of discretion, it is not a right to counter-restitution in the true sense.

B. *Election Between Remedies*

Tang Man Sit v *Capacious Investment Ltd*[62] established that the plaintiff has to elect between compensation for losses occasioned by the wrongdoing and restitution. The Privy Council held that both are inconsistent remedies. The decision has been criticised by Birks[63] who argues that there is really no inconsistency and what we are only guarding against is double recovery. If the plaintiff could recover the defendant's gains when he suffered no loss, there is no reason to say that there is inconsistency where the plaintiff has also suffered a loss and wants the defendant's gains and to disgorge his profits.

It is submitted that there really is no inconsistency since one is concerned with the defendant's gain and the other with the plaintiff's loss. The Law Reform Commission agreed with Birks that it is a misnomer to have an election requirement. Provided that one takes account of the other, there is no inconsistency or double recovery in allowing both restitution and compensation to be awarded.[64]

C. *Deterrence and Moral Culpability*

'...the law is mocked if it enables a man to profit from his own wrongdoing.' – Diplock LJ in McCarey v *Associated Newspapers.*[65]

The need for some measure of deterrence is necessary in many of the civil wrongs where it is impossible or difficult to prove a loss and yet there is a need to express strong disapproval and discouragement. In *Stoke-on-Trent*, there was no way the city could protect itself from infringement of its monopoly since restitutionary damages were disallowed and it was not possible to prove the financial loss suffered. In the recent Law Reform Commission Report,[66] it was recommended that legislation should provide for restitutionary damages where a defendant had committed a tort, an equitable wrong or a statutory civil wrong, and his conduct showed a

62 [1996] AC 514.
63 Birks, 'Inconsistency Between Compensation and Restitution' (1996) 112 LQR 375.
64 Law Reform Commission Report, *supra*, note 1, at paras 1.64–1.72.
65 [1965] 2 QB 86 at 107.
66 Law Reform Commission Report, *supra*, note 1.

'deliberate and outrageous disregard of the plaintiff's rights'. The recommendation was made in the line of rationalising the approach towards exemplary damages by confining exemplary damages where the defendant had deliberately and outrageously disregarded the plaintiff's rights. Breach of contract was excluded for the usual reasons against awarding exemplary damages.

The Law Reform Commission's view is not new. The availability of account of profit for breach of confidence, as discussed earlier, turns on whether the breach is deliberate. Academics including Birks have argued that restitutionary damages are most effective not only to undo a particular instance of acquisition wrongdoing but also as a deterrent to others from engaging in a course of conduct.[67] He argues that where the defendant's conduct is deliberate, restitutionary damages should be allowed unless the court holds that suppression of that form of intentional unlawful profit is not necessary or desirable. It may be pointed out that exemplary damages may act as a better deterrence since taking away the gain is only a disincentive, not a deterrent.[68]

However exemplary damages are objectionable on a number of grounds, especially its indeterminate nature which can easily descend to "palm tree" justice. Restitutionary damages are at least quantifiable. Also it is questionable whether we should use civil law to punish. Birks argues that all awards punish the defendant to a greater or lesser extent.[69] This is misleading. The aim of compensation is to do justice between the parties by awarding compensation to the plaintiff who has suffered a loss. Punishment is to promote general welfare.

The current position taken by the case-law is that moral culpability is not a basis for imposing liability. Steyn LJ in *Surrey CC* rejected the deliberate breach of contract as relevant on the ground it would lead to greater uncertainty in the assessment of damages in commercial and consumer disputes. The Court of Appeal in *AG* v *Blake* held that wilfulness of the breach of contract was not by itself a necessary or, for that matter, sufficient factor to found liability. The recourse to moral culpability on the defendant's part is unattractive conceptually. It is not self-evident what degree of fault is to be attributed

67 Birks, Civil Wrongs, *supra*, note 6, at 94-95.

68 As pointed out by Lord Diplock in *Broome* v *Cassell* [1972] AC 1027, 'to restrict the damages recoverable to the actual gain by the defendant contemplating an unlawful act with the certainty that he had nothing to lose to balance against the chance that the plaintiff might never sue him, or if did, might fail in the hazards of litigation. It is only if there is a prospect that the damages may exceed the defendant's gains that the social purpose of this category is achieved – to teach a wrongdoer that tort does not pay.'

69 Birks, Civil Wrongs, *supra*, note 6, at 79.

to him before he is so liable. *Stoke-on-Trent* is a clear example of a cynical wrongdoer but not in the other cases. If a builder finds that he is unable to fulfil all the contracts at the same time due to unforeseen events, and seeks to get out of some of them, is he a cynical wrongdoer?

V. Whither Legislation?

A. *Confiscation of Benefits*

Should the entire area be left to legislation providing for confiscation of the benefits of the crime or wrongdoing? The main statutes in Singapore are Corruption (Confiscation of Benefits) Act[70] and Drug Trafficking (Confiscation of Benefits) Act.[71] There was some hint in *AG* v *Blake* where the Attorney-General sought relief not as a nominal plaintiff representing the Crown, but as a guardian of the public interest. The Court of Appeal held that he was entitled to intervene by instituting civil proceedings, in aid of the criminal law, to uphold the public policy of ensuring a criminal did not retain profit directly derived from the commission of his crime. The court's jurisdiction extended to enforcing public policy with respect to the consequences of the commission of that crime, including restraining receipt by the criminal of a further benefit as a result or in connection with that crime.

The Court of Appeal in *Halifax Building Society* was influenced by the fact that Parliament had enacted the English Criminal Justice Act 1988 where the Crown Court may confiscate any gain which a criminal would otherwise derive from his crime. One Thomas came under the Act and a confiscation order was made. Whatever the outcome of the appeal, he would not have benefited from his crime.[72]

However it is submitted that the matter should not be left entirely to confiscation legislation. Taking this reasoning to its logical conclusion, any form of restitutionary remedy in *AG of Hong Kong* v *Reid* and in *Thahir* v *Pertamina* should not be granted if there was legislation providing for the confiscation of corrupt benefits. However if an order was indeed made under such legislation, it is unenforceable in New Zealand as a penal law, and the Crown would be powerless to lodge caveats against the landed property which was the traceable proceeds of the bribe. Similarly, the Indonesian state corporation would be unable to enforce the legislation here

[70] Cap 65A (1990 Ed).
[71] Cap 84A (1990 Ed).
[72] In the UK, the 1988 Act was amended by the Proceeds of Crime Act 1995.

even if there is an order for the confiscation of the benefits in Indonesia, in the absence of any treaty. All this suggests that judicial creativity is necessary to create a solution. Where the benefit derived from Thomas' (in *Halifax*) wrongdoing is stashed away in another jurisdiction, the only way is for the bank to obtain a judgment in its favour and then enforce it in another jurisdiction. If all that one is relying on is the confiscation of benefits laws, it is plainly unenforceable in another jurisdiction, being a penal law.[73] This is a general problem in enforcement of judgment in private international law.

B. *Restitutionary Principles*

Restitutionary principles to deprive the defendant of the proceeds of his crime may not fall within restitution but into public law. The 'Son of Sam' statutes which were enacted in the United States were the result of the moral revulsion engendered by the perception that criminals were receiving financial gain from their literary ventures.[74] In the early 1970s, one David Berkowitz committed a number of murders, signing himself as 'Son of Sam'. The murders were known as the 'Son of Sam' murders. Berkowitz was eventually arrested and he entered into an arrangement with publishers to receive a sum in exchange for the rights to the story of his arrest. This created a public outcry and New York enacted legislation confiscating the literary profits for the benefit of the victim. This was soon followed by other states.

It is not obvious that literary profits are directly analogous to the proceeds of crime. In fact, instinctively there is a distinction between commission of the crime and the production of a literary work. The benefit derives directly from the literary activity, and only indirectly from the offence. The criminal receives his benefit not from committing the crime but from entering into a lawful contract. *AG* v *Blake* was unusual in that the publication was itself a crime, being in breach of the Official Secrets Act 1989.

[73] It is interesting to note that in the amended 1988 UK Act, s 71(1C) contemplates that where the victim of the crime would bring civil proceedings for "loss, injury or damage sustained", the court would have the power to make an order for confiscation. It was the intention of the provision that the court would make a confiscation order which is the net of any award to the victim, since the amount of compensation is likely to be less than the net assets. However the provision does not envisage that the victim is able to bring an action for disgorgement of the proceeds of the crime.

[74] See McClean, "Seizing the Proceeds of Crime: The State of the Art" (1989) ICLQ 334; Freiberg, 'Confiscating the Literary Proceeds of Crime' [1992] Crim LR 96.

VI. Proprietary Restitution for Wrongdoing

A. *Justifications for Proprietary Remedies for Wrongdoing*

Once we have determined that restitution is a proper response to the wrongdoing, the next question is whether the response should be proprietary or personal. A restitutionary proprietary claim is one which removes from the defendant an equitable right over the assets received by him at the expense of the plaintiff and is not explicable on the basis of consent or other events. Here we are concerned only with the situation where what is relied on is the wrongdoing and not restitution of the benefit obtained by subtractive unjust enrichment.[75] The restitutionary proprietary remedy generated can only be in the form of a constructive trust or an equitable charge since its function is to make the defendant give up to the plaintiff a gain derived from elsewhere. Resulting trust has no role to play at all since it does not operate to return the asset whence it came.[76]

There are many justifiable fears regarding the adverse effects of proprietary remedies on the legitimate interests of the third parties on the recipients' property. Strategies have been proposed to control the proprietary restitution:

(1) 'undestroyed proprietary base', *ie,* the plaintiff must show that he has a proprietary right in the subject-matter right from the outset and that that right has not been extinguished by the subsequent events;[77]

(2) policy-motivated, *eg*, whether the plaintiff took the risk of the defendant's insolvency;[78] and

(3) conscience of the defendant. The last strategy is propounded by Lord Browne-Wilkinson in *Westdeutsche Landesbank Girozentrale* v *Islington LBC* in his formulation of the remedial constructive trust:[79]

[75] For a recent discussion on the basis for the proprietary remedy in subtractive unjust enrichment, see Birks, "Trusts Raised to Reverse Unjust Enrichment: *The Westdeutsche Case*" [1996] RLR 3.

[76] Chambers, *Resulting Trusts* (1997).

[77] Birks, "Establishing a Proprietary Base (*re Goldcorp*)" [1995] RLR 83.

[78] *Supra*, note 7, at 95.

[79] [1996] 2 WLR 802 at 837, 839.

> Under an institutional constructive trust, the trust arises by operation of law as from the date of the circumstances which give rise to it: the function of the court is merely to declare that such trust has arisen in the past. The consequences that flow from such trust having arisen (including the possibly unfair consequences to third parties who in the interim have received the trust property) are also determined by rules of law, not under a discretion. A remedial constructive trust, as I understand it, is different. It is a judicial remedy giving rise to an enforceable equitable obligation: the extent to which it operates retrospectively to the prejudice of third parties lies in the discretion of the court...
>
> Although the resulting trust is an unsuitable basis for developing proprietary restitutionary remedies, the remedial constructive trust, if introduced into English law, may provide a more satisfactory road forward. The court by way of remedy might impose a constructive trust on a defendant who knowingly retains property of which the plaintiff has been unjustly deprived. Since the remedy can be tailored to the circumstances of the particular case, innocent third parties would not be prejudiced and restitutionary defences, such as change of position, are capable of being given effect...

With this recent judicial pronouncement, albeit only *dicta*, a great deal of excitement has been generated over the novel remedial constructive trust in England. Briefly, a remedial constructive trust is an order granted by the court that will not affect innocent third parties. The court will not make such an order unless it meets the justice of the particular case. An institutional constructive trust, in contrast, has proprietary effect from the date of the underlying facts, irrespective of a court order. The key element to the remedial constructive trust is the discretion of the court.[80] No doubt the boundaries of the discretion have to be laid down on a case by case basis. Recently it was established in *Re Polly Peck International*[81] that a remedial constructive trust cannot be used to confer a priority not accorded by the insolvency regime. The facts are stated in greater detail below. The applicants sought leave of court to commence proceedings against PPI (which was insolvent) under the Insolvency Act for trespass and submitted that there was at least an arguable case that a remedial constructive trust should arise. The Court

[80] See Paciocco "The Remedial Constructive Trust: a Principled Basis for Priority over Creditors" (1989) 68 CBR 315 at p 321; Gardner, "The Remedial Constructive Trust: the Element of Discretion" in Birks, *The Frontiers of Liability*, vol 2 (1994), at 186.

[81] CA, unreported, 7 May 1998, LEXIS Transcript.

of Appeal, reversing the decision of Ratnee J, held that the intervening insolvency of PPI meant that there was not even an arguable case for granting a remedial constructive trust. The effect of the statutory scheme applicable on an insolvency was to shut out a remedy which would, if available, have the effect of conferring a priority not accorded by the provisions of the statutory insolvency scheme.

After *Polly Peck International*, the scope for the remedial constructive trust appears to be very much diminished. It will be argued that restricting the constructive trust is desirable. It is really impossible for the courts to weigh the abstract justice of each claimant to determine whether property rights are imposed without descending to "palm-tree justice". Also, property rights are too important to be varied by a general discretion. The only exception that is justifiable is in the case of bribes or corruption where policy may demand that a remedial constructive trust be imposed.

B. *Bribery or Corrupt Benefits*

This is an area where controversy rages over discovering a principled justification (in addition to a purely policy justification) for the reaching the decisions in *Attorney General of Hong Kong* v *Reid* and in *Thahir* v *Pertamina*.[82] These cases on bribery and corruption represent the most important developments in this area in suggesting that the proprietary remedy is institutional. However, it is argued in this part that the constructive trust imposed is in truth only remedial and not institutional.

In *AG of Hong Kong* v *Reid,* the corrupt Director of Public Prosecutions in Hong Kong, in the course of his career with the legal service, had in breach of fiduciary duty owed to the Crown, accepted bribes in return for obstructing the prosecution of certain criminals. With the bribes, he used to purchase two properties in New Zealand. The Attorney-General of Hong Kong lodged caveats in New Zealand against the properties and applied to renew the caveats. The judge at first instance refused his application on the ground that the Crown had no equitable interest in the property. The Privy Council held that the Crown had an equitable interest in the properties; the corrupt fiduciary held the properties on trust for the Crown as they represented bribes received by him. This was a departure from the earlier English Court of Appeal decision in *Lister* v *Stubbs*,[83] which held

[82] *Eg*, see Birks, 'Obligations and Property in Equity: *Lister* v *Stubbs* in the Lime Light' [1993] LMCLQ 30; Beatson, 'Proprietary Claims in the Law of Restitution' (1995) 25 Can Bus LJ 66; Crilley, 'A Case of Proprietary Overkill' [1994] RLR 57.

[83] (1890) 45 Ch D 1.

that the principal only had a personal remedy against the defaulting fiduciary. The Privy Council approved of Lai Kew Chai J's decision in *Thahir* v *Pertamina*[84] (which had not yet been heard on appeal) which had disapproved *Lister* v *Stubbs* as undesirable and unjust.

In *Thahir* v *Pertamina*, interpleader proceedings were taken out and the trial judge found that all the 17 ACU deposits denominated in deutschemarks were bribes which the contractors had paid to General Thahir in return for payments made to them by Pertamina. The Court of Appeal, affirming the decision of Lai Kew Chai J, held that Pertamina's claim was governed by Singapore law, and that the bribes were held on constructive trust for Pertamina. In addition, General Thahir's wife, by reason of her complicity and involvement in the transfer of the deposits to the account in both their joint names, also became a constructive trustee. When she became the sole owner of the deposits she continued to hold them on constructive trust for Pertamina.

In *AG of Hong Kong* v *Reid*, the Privy Council held that the maxim 'equity considers as done that which ought to be have been done' applied. The Privy Council reasoned that as soon as the bribe was received by the bribee, it should have been paid over to the principal and hence the fiduciary was treated as a constructive trustee of it. This treats the constructive trust imposed as exclusively institutional. Similarly, Birks argued that applying the doctrine of *Walsh* v *Lonsdale*[85] which confers an immediate equitable property on the person entitled, the bribee was bound at the moment he received the bribe to hand it over to the principal and since equity regards as done that which ought to have been done, the bribe ought to be given to the principal.[86] That was his proprietary base at the head of a chain of substitutions that led to the property in New Zealand. With respect, these arguments really beg the question. The bribee had no authority to receive the payments for his employer's account and had no authority to mix them and use for his own purposes. It is only if the bribee is under an obligation specifically enforceable to deliver up the bribe that the maxim applies to make him a constructive trustee of the assets.

Lord Templeman advanced three further arguments in support of a proprietary remedy: first, the dishonest fiduciary should not be able to retain profits from investing moneys made from a wrongful gain; second, to prevent the bribee from whisking the asset to some Shangri La which hides bribes and other corrupt moneys; and third, an unsecured creditor should not be in

[84] [1993] 1 SLR 735, reported as *Sumitomo Bank* v *Thahir & ors*.
[85] (1882) 21 Ch D 9.
[86] [1995] RLR 83.

a better position than his debtor who is the wrongdoer *vis-à-vis* the victim. Each of these reasons has to be scrutinised carefully.

The first is a powerful policy reason as to why the corrupt fiduciary should be stripped of his benefits from his wrongdoing. However, by imposing a proprietary remedy, the fiduciary's general creditors are similarly deprived and yet they have done nothing wrong. By definition, the general creditors have given value to the bribee, swelling his assets. There is no reason why the bribee should not be personally liable to account for the profits made from investing in the wrongful gain and not merely the bribe. The aim of preserving the loyalty of fiduciaries can be equally achieved by a personal response. In respect of the third reason, all the unsecured creditors will stand to lose and the only question is by how much. As a class, unsecured creditors are treated unequally compared to those who hold proprietary rights. The source of any arbitrariness comes from the nature of proprietary rights. Proprietary rights have a specific subject and the specificity of proprietary rights will inevitably lead to inequality among claimants. Goff & Jones argues for a proprietary remedy on the grounds that the plaintiff has not taken the risk of insolvency.[87] This is consistent with their policy-based theory of restitutionary proprietary remedy.

The second argument is more convincing. It is a legitimate concern that a personal remedy might be frustrated by the assets being taken out of the jurisdiction. Lord Templeman was concerned that the bribe could be invested in the bribee's Shangri-La, frustrating the recovery of the assets. This may be a general problem in the enforcement of foreign judgments but applies with force in the case of bribery which is "an evil practice which threatens the foundations of any civilised society' and it is repugnant to public policy that the bribee is able to frustrate the recovery of assets so easily".[88] Hence a proprietary remedy will be granted not only where a personal remedy is demonstrably inadequate to effectively deprive him of retaining any enhancement in the value of what he has achieved. Then reliance on the

[87] *Supra*, note 7, at 95. A similar view is taken by Paciocco, "The Remedial Constructive Trust: a Principled Basis for Priority over Creditors" (1989) 68 CBR 315. This view is convincingly refuted by Burrows, *Law of Restitution* (1993) at 42 where he argues that even if ordinary creditors consciously take the risk of the defendant's insolvency, there is no reason why this is a valid distinction. If a restitutionary proprietary remedy is denied, the general creditors will receive a windfall, this applies in all cases of unjust enrichment and this is not an argument to distinguish some unjust factors from others, and I would add, from the types of wrongs.

[88] *Per* Lord Templeman in *Reid*, *supra*, note 11, at 330-331.

remedial constructive trust will be necessary[89] In most cases, making the dishonest fiduciary to disgorge all his ill-gotten gains including any enhancement in value will be sufficient. However in others, such a remedy is not enough. In *Reid*, the Attorney-General of Hong Kong wished to lodge a caveat in the Land Registry in New Zealand to prevent any dealing of the property pending the outcome of the proceedings. This is a sort of interlocutory remedy, albeit of a stronger nature when a proprietary right is at stake. If all that the Crown had was a personal remedy against the defendant, no caveats may be lodged against the property since the Crown would not have any equitable interest in the property. The use of the remedial constructive trust is the most apt to protect the plaintiff's rights.[90]

C. *Breach of Fiduciary Duty and Contract*

Traditionally, the preference for a proprietary right is accorded not only in cases of bribes but in all cases of receipt of benefit in breach of fiduciary obligation. An authority that is usually applied for the proposition that the remedy of constructive trust is awarded for breach of fiduciary duty is *Keech* v *Sandford*[91] where a trustee who renewed for his own benefit a lease which the landlord was not prepared to renew to the trust was held to hold the lease on constructive trust for the trust. This was an eighteenth century decision but it produced a line of authority concerning not only when the fiduciary may obtain for his own benefit a lease held by his principal, but also when a fiduciary may hold a benefit obtained for himself on constructive trust for the beneficiary. As I have argued in Part IV, it is appropriate to relax the penal attitude displayed by the authorities and liberalise the kinds of remedies for fiduciaries, especially in non-trustee fiduciary contexts. Recent case-law exemplifies the trend to identify the specified duties rather than an entire relationship. Outside corruption and bribery cases, there really is no policy reason for imposing proprietary remedies.

Goode argues that a proprietary remedy for restitution for wrongs is only justifiable where there are deemed agency gains, *ie*, gains which the defendant receives through improperly engaging in dealings on his own account which, if he entered into them at all, should be engaged in for the benefit of the

[89] Waters, "The Nature of the Remedial Constructive Trust" in *Frontiers of Liability, supra,* note 80, at 165; Tjio H, "The Personal and Proprietary Distinction" [1993] SJLS 198; *cf* Birks, "Proprietary Rights as Remedies" in *Frontiers of Liability*, vol 2 (1994) at 214.

[90] For a discussion as to the priority claims that may arise outside insolvency and the other reasons for wanting to classify a given liability as a trust, see Elias, *Explaining Constructive Trusts* (1990) at ch 5.

[91] (1726) Sel Ch Cas 61.

plaintiff[92] The gains thus obtained will be treated in equity as if they had in fact been procured for the principal.[93] This was cited with approval recently by the majority of the Supreme Court in *Soulos* v *Korkontzilas*[94] where McLachlin (La Forest, Gonthier, Cory and Major JJ concurring), after considering the case-law in the commonwealth jurisdictions and the seminar decision in *LAC Minerals* v *International Corona*,[95] held that four conditions to be satisfied before a constructive trust may be imposed are:

(1) the defendant must be under an equitable obligation in relation to the activities which gave rise to the assets acquired by the defendant in breach his equitable obligations;

(2) the assets must have resulted from deemed or actual agency activities of the defendant in breach of the equitable obligations;

(3) the plaintiff must show a legitimate reason for seeking a proprietary remedy; and

(4) there are no factors rendering the imposition of constructive trust unjust.

In that case, a real estate broker acted for a potential purchaser of a commercial property. When the deal with the seller fell through, he arranged to purchase in his wife's name and the purchaser sought a declaration that the property be held on constructive trust for him. He abandoned his claim for damages since the property fell in value. He claimed that the property had special value since one of the tenants was a bank and to be a landlord of the bank had special significance in the community. The majority of the Supreme Court held that all four conditions were satisfied, since the broker breached his equitable obligation by putting himself in a conflict of interest, and the property acquired by the broker was the result of his breach. A constructive trust was appropriate since the purchaser had a personal reason to acquire the property and it was necessary to ensure that agents remain faithful to their duty of loyalty.

92 Goode, "Property and Unjust Enrichment" in *Essays on the Law of Restitution* (Burrows ed, 1991), ch 9; "The Recovery of a Director's Improper Gains: Proprietary Remedies for Infringement of Non-Proprietary Rights", *Commercial Aspects of Trusts and Fiduciary Obligations* (McKendrick ed, 1992), ch 7.

93 See also Worthington, *Proprietary Interests in Commercial Transactions* (1996) at 118 where she suggests that one party will only become the equitable owner of property belonging to another if there requirements are satisfied: (1) he must be under a mandatory and (2) unconditional personal obligation to transfer (3) identifiable property to the first party.

94 (1997) 146 DLR (4th ed) 214.

95 (1986) 61 DLR (4th ed) 14.

There are obvious difficulties with the manner in which the majority applied the concept of a legitimate advantage of seeking a proprietary remedy. The defendant had put himself in a position of conflict of interest and retained for himself a benefit of the transaction. However the plaintiff's legitimate reason is but a personal motivation of a purchaser which is not sufficient to make the property unique. Also there is no explanation how imposing a constructive trust would ensure that agents and other fiduciaries remain faithful to their principals where a personal remedy would equally suffice.

For pure breaches of contract, there really is no scope for the imposition of the remedial constructive trust. In *Re Goldcorp*, the Privy Council refused to raise proprietary interest by way of a flexible response to the customers' interest. In that case, investors purchased gold bullion from Goldcorp under a contract for future delivery. The contract provided that the gold was stored in a vault on their behalf and physical delivery was possible with seven days' notice. No allocation of the gold was made and the investors had a certificate of ownership verifying the ownership. In breach of contract, Goldcorp did not retain sufficient bullion and went into liquidation. The investors tried unsuccessfully to obtain a beneficial interest over the remaining gold bullion in the stock. The Privy Council held that Goldcorp was not a fiduciary and the so-called fiduciary relationship was nothing beyond those assumed under the contracts of sale with collateral promises that the company kept a separate stock of bullion. These obligations were not different from those derived from the contract and to introduce fiduciary obligations would be introducing a new dimension into such a relationship that would have adverse consequences.

In *Re Goldcorp*, it is really impossible for the court to assess the abstract justice of the case to determine whether the investors or the bank (which was the holder of the equitable charge claiming in priority over the investors) should benefit. The bank is more able to absorb losses but the losses are ultimately passed on to its customers. Also in *Re Goldcorp*, there is no reason to protect the investors when they can afford speculative investment in which losses and gains could be made. The proponents of the remedial constructive trust argued that it enables flexibility in the remedies but property rights are too important to be left to the discretion of the court.

There was some suggestion that the remedial constructive trust was available for trespass to land in *Re Polly Peck International* though the decision was ultimately reversed on a different ground. In *Re Polly Peck International*, the Court of Appeal decisively rejected the argument that it was open to impose on the assets of the insolvent company in administration a remedial constructive trust so as to give the applicants a proprietary interest. It was an extraordinary case. The applicants asserted that a piece of property in Cyprus was owned by them, and that land had been expropriated by the Turkish Federated State following an invasion. The claim was that PPI

had, knowingly, permitted its subsidiaries to illegally occupy the land and derived substantial profits from such occupation. The shares in the subsidiaries of PPI were ultimately sold to Learned Ltd. PPI became hopelessly insolvent and the administrators held the proceeds of the sale. The applicants sought leave of court to commence proceedings against PPI under the Insolvency Act 1986. They had to show an arguable case before leave could be granted. The trial judge held that the statement of claim disclosed a seriously arguable claim against PPI. The applicants had good causes of action for trespass against the subsidiaries and if the amount of the proceeds of the sale had been increased by the fact that subsidiaries had benefited from the alleged trespass, PPI obtained the benefit of the increase from Learned Ltd. Against PPI, as it knew that its subsidiaries were exploiting the properties to which the applicants claimed title, and PPI encouraged such exploitation and had in fact benefited from the exploitation, it should be bound to disgorge. The Court of Appeal reversed the decision on the ground that a remedial constructive trust could not be imposed to upset the insolvency regime.

VII. Conclusion

There are many issues to be resolved in this area. A study of the circumstances in which gain-based damages are awarded for wrongs indicates that they should be awarded across the board for all types of wrongdoing. They are all founded on the principles of the necessity of deterrence, which are found in all kinds of wrongdoing, and in other cases, the risk of under-compensation. The traditional justifications of proprietary wrongs, breach of fiduciary duties, and moral culpability do not adequately explain why lines are drawn as they are in case law. It is unfortunate that the area is clouded by the use of various terminology which are in fact restitutionary damages in disguise. Instead of limiting the kinds of wrongdoing for which restitutionary damages are awarded, we need is to develop limitations to restitutionary damages by rules of remoteness and causation. This is especially in the context of fiduciaries, where the focus then will be on the kind of relationship between the parties, and not merely on the label of "fiduciary". I have cautioned against an excessive reliance on legislation as providing the perfect solution.

Whether the response should be personal or proprietary has to be answered. This is a fast-developing area that poses challenges in the volume and complexity of some of the key issues. The exact ramifications of the remedial constructive trust based on the conscience of the defendant envisaged in *Westdeutsche* v *Islington LBC* has yet to be worked out fully. Early indications show that the remedial constructive trust cannot be utilised to upset the statutory prescribed insolvency regime but there are many other priority

claims outside insolvency. It is submitted that the way ahead is to restrict the remedial constructive trust as a restitutionary proprietary remedy to the bribery or corruption cases where the plaintiff demonstrates that he has a legitimate interest to have his expectations protected. Outside this limited category, the adoption of the remedial constructive trust leads to too much uncertainty and is undesirable.

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