Chapter - VII
ENRICHMENT BY WRONGDOING

7.1 Introduction

The wrongdoing principle is claimant-based: the claimant obtained his contractual rights through a wrongful act. The ‘substantive fairness principle’ has a mixed basis: the value of the claimant’s contractual rights is greater than the value of the defendant's rights. In practice, however, it is often difficult to tell which of these principles (if any) best explains particular rules. In part, this is because many of the rules in this area can plausibly be explained on more than one of these grounds. Consider the rule that a contract signed under duress—for instance, a contract signed at gunpoint—is invalid. The defendant in such a case can plausibly argue that she never consented to the contract. But she can also plausibly argue that the claimant obtained his apparent rights by a wrongful threat and (in most cases anyway) that the actual terms of the agreement are unfair. The end result is that there may be more than one good reason for refusing to enforce such a contract. In principle, this is not a problem, but in practice it exacerbates the difficulty of disentangling the relevant concepts, and may help to explain why the law in this area is complex, if not actually inconsistent, in certain respects.

Another reason it is difficult to tell which principle best explains any given rule is that these principles are often subject to overlapping definitions. For example, lack of consent is often defined in terms of wrongdoing (and vice versa); thus it is often said that consent is negated by illegitimate (i.e. wrongful) pressure or, alternatively, that it is wrongful to do something that impairs another's consent. As for substantive unfairness, it is often defined in terms of lack of consent and wrongdoing: a contract is substantively fair, it is often said, if it is procedurally fair.
A third reason that commentators disagree about how to explain the rules on excuses is that the answer has implications for a larger debate in contract law regarding the relative significance of procedural as opposed to substantive fairness. According to classical theory, while procedural matters of the kind that are the focus of consent and wrongdoing principles are properly the concern of the law, the substantive outcome of a contract is purely a matter for the parties. In this view, the law regulates the way bargains are made in the marketplace, leaving the parties to insert whatever content they choose into those bargains. In short, even if it is possible to define substantive fairness, such a definition is of no concern to the law of contract. But as we have already seen, this classical view is frequently criticized, both as an account of what the courts actually do and as a prescription for what they should do. The law on excuses—particularly the rules on duress, undue influence, and unconscionability plays a major role.

The law in this area thus raises difficult issues. For the moment, it is sufficient to make the following observations. First, whatever philosophers may say about the meaning of consent, wrongdoing, and substantive fairness, these concepts are regularly employed in ordinary conversation and, indeed, in legal reasoning. Since judges and others appear to ascribe meaning to them, it is a good starting point to assume that these concepts do in fact matter. Secondly, it would be surprising if the courts were not motivated by concerns about consent, wrongdoing, and substantive fairness. In the cases of consent and wrongdoing this proposition is uncontroversial; these are widely recognized as fundamental moral concepts.

Nonetheless, even if it is agreed that judges might hesitate to set a contract aside solely because it is substantively unfair (assuming they had the power to do this), it would be surprising if they disregarded this concept in instances when it was linked to a claim that the defendant’s consent was impaired or that the claimant acted wrongly, even in cases where such impairment or wrongdoing might not alone be sufficient to justify invalidity. The idea that it is
wrong to take advantage of another's vulnerability—for that is how these situations would ordinarily be described is too ingrained to be ignored entirely by the law.

Finally, it should be mentioned that there is an important sense in which the law on excuses is arguably not a part of the law of contract, strictly understood, or at least not uniquely a part of contract law. A contractual obligation that was induced by a wrongful threat or a fraudulent representation may be set aside by a court. But the same is true of a will, a declaration of trust, or a decision to legally change one's name—yet none of these acts are contracts. So too, an ordinary transfer of property will be undone if it was induced by a wrongful threat or fraud.

The core idea of fiduciary duty is the assumption of responsibility for the property or affairs of others. Parallel developments at common law and in equity yielded the recognition of a duty of care of those in analogous positions of being entrusted with another's property or affairs, including bailees, carriers, trustees, directors and agents. The duty to take care of another's interests in such circumstances is clearly established, although the exact standard of liability may vary from case to case Hederson v. Merrett Syndicates Ltd.\(^1\) and Bristol and West Building Society v. Mothew\(^2\). Breaches of this duty of care are not breaches of fiduciary duty: It is obvious that not every breach of duty by a fiduciary is a breach of fiduciary duty. Breach of fiduciary obligation, therefore, connotes disloyalty or infidelity. More incompetence is not enough. A Servant who loyally does his incompetent best for his master is not unfaithful and is not guilty of a breach of fiduciary duty. Bristol and West Building Society v. Mothew.\(^3\)

It is with breaches of the obligation of loyalty with which we are now concerned. Where the money or property of another is entrusted to a person,

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\(^1\) (1995) 2 AC 45 at p. 205
\(^3\) Id. at p. 16, 18.
equity has always been suspicious of the temptations which might thereby arise. A restitutionary response has therefore been recognized and is apt for two reasons. First, infidelity is likely to result in enriching behaviour for the person entrusted with the money or property of another. Secondly, the policy of deterrence or prophylaxis weight heavily with the court. As Professor Jones argued in his seminal article, ‘Unjust Enrichment and the Fiduciary’s Duty of Loyalty’.4

The implications of equity’s rule are far-reaching. Once a fiduciary is shown to be in breach of his duty of loyalty he must disgorge any benefit gained even though he acted honestly and in his principal’s best interests, even though his principal benefited as well as he from his conduct, even though the benefit was obtained through the use of the fiduciary’s own assets and in consequence of his personal skill and judgment.

In a number of cases a too-mechanical application of these principal has led to unjust results.

7.2 Who is Fiduciary?

The categories of fiduciary relationships which give rise to a constructive trusteeship should be regarded as falling into a limited number of strait jackets or as being necessarily closed. They are, after all, no more than formulae for equitable relief.

No should explicit or implicit consent necessarily be an exhaustive guide to fiduciary responsibility.

For example, in the leading case of Boardman v Phipps,5 the solicitor to a will trust and a beneficiary under the trust staged a skilful takeover of an ailing textile company in which the trust held a minority shareholding. Using considerable business acumen the two men turned the fortunes of the company

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4 (1968) 84 LQR 472, at p. 474.
5 (1967) 2 AC 46.
around. This was done with the acquiescence of the active trustees, although no formal consent was ever obtained (nor due to the incapacity of one of the trustees could it ever have been obtained). In a claim brought by one of the other beneficiaries, Wilberforce J labelled the two as ‘self-appointed agents’ for the trustees. The majority of the House of Lords agreed that the two were in a fiduciary position, and were in breach of it by using information and an opportunity which came to them by reason of their relationship with the trust. However, they did not approve of the appellation of ‘self-appointed agents’. Lord Guest, for example, preferred to say that they placed themselves in a special position which was of a fiduciary character. It is clear that the ascription of fiduciary responsibility is ultimately a matter for the courts. Regard is had to the underlying consensual relationship, including the terms of any contract between fiduciary and principal. This contractual matrix may exclude or modify the full rigour of the fiduciary regime. However, in the majority of cases the relationship is firmly bottomed on the consent or assumption of responsibility by the alleged fiduciary alone.

### 7.3 Fiduciary Relationships

Closely analogous to these cases are those involving what Courts of Equity would call a ‘fiduciary relationship’, such as the one that exists between a trustee and a beneficiary. In these cases, which often involve contractual relationships, the duty not to abuse the fiduciary position includes a requirement to disclose all material facts. The same applies to many ‘undue influence’ cases which, it is important to emphasise, are not solely concerned with what might be called undue influence in the ordinary sense. However, in both these and other relevant cases, the duty to disclose is obviously subordinate to the general duty to not abuse the position of trust or exploit the relationship between the parties.

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6 (1964) 1WLR 993, at p. 2007.
7 Id. at p. 118.
7.4 The Obligation of the Fiduciary

If the core obligation of the fiduciary is loyalty, the paradigm instance of breach of fiduciary duty is non-disclosure. The case law divides into two broad categories. First, transactions between the principal and fiduciary, secondly, transactions or dealings by the fiduciary with third parties, whether purportedly done on behalf of the principal and fiduciary. Secondly, transactions or dealings by the fiduciary with third parties, whether purportedly done on behalf of the principal or not. As a general rule it may be stated that if the fiduciary makes full disclosure of all the circumstances to the principal or not. As a general rule it may be stated that if the fiduciary makes full disclosure of all the circumstances to the principal and the principal gives informed consent to the dealings, the transaction to the principal and the principal gives informed consent to the dealings, the transaction will stand in either category. There is no room for a detailed survey of the case law and the content of the obligation here. Where the fiduciary deals directly with its principal, the burden of proof is upon the fiduciary to demonstrate affirmatively that the transaction was fair and that in the course of negotiations he made full disclosure of all the facts material to the transaction. Any non-disclosure by the fiduciary will entitle the principal to rescind the transaction. This is a leading exception to the general position in English law that non-disclosure does not vitiate transactions. If rescission is no longer possible, in the alternative the fiduciary will be liable to account may in appropriate circumstances be reinforced by a proprietary restitutionary remedy.

A significant recent statement of authority came in Guinness plc v. Sauders.\textsuperscript{9}
Guinness sought to recover 5.2 million paid to ward, an American attorney and former director of the company, made at the time of the controversial bid by Guinness to take over Distillers. Ward together with the then chief executive, Saunders, and another director, Roux, formed a take-over subcommittee of the Board. That subcommittee agreed to pay Ward 0.2 percent of the ultimate value

\textsuperscript{9} (1990) 2 AC 663.
of the bid if successful for his services in connection with the bid. This yielded 5.2 million. It was ultimately held by the House of Lords that Guinness’s articles of association only empowered the board of directors to award such remuneration Accordingly the contract was void for want of authority of the sub-committee. Lord Goff of Chievely stated.

### 7.5 Remedies for Breach

The characteristic remedial response is that a fiduciary must disgorge the benefits derived from his breach of duty. Remedial flexibility is demonstrated by the two leading cases on the liability of company promoters.

*In Erlanger v. New Sombrero Phosphate Co.*\(^{10}\) a syndicate of promoters purchased the lease for a West Indian Island for $55,000. They promoted a company with the object of exploiting the island's phosphate reserve. Subsequently the syndicate sold the island to the company for $110,000. They failed to disclose the inflated price to the investor. The House of Lords unanimously held that the promoters stood in a fiduciary position towards the company and owed it a duty to make full disclosure of the circumstances of their acquisition of the property. The company was held entitled to rescind the contract and to restitution of the property. The company was held entitled to rescind the contract and to restitution of the purchase price, conditional upon giving up possession of the island and paying over any profits made in the interim.

*In Gluckstein v. Barnes,*\(^{11}\) a syndicate purchased the Olympia Exhibition Hall for $140,000. They subsequently promoted a company to which to sell the property for $180,000. The prospectus disclosed a profit of $40,000, but failed to disclose a further profit of $20,000 made in relation to the property. The House rejected an argument that the only remedy was rescission, relying upon

\(^{10}\) (1878) 3 App Cas 1218.

\(^{11}\) (1990) AC 240.
the authority of *Hichens v. Congreve*.\textsuperscript{12}

The claim to rescission in Erlanger can be rationalised either as based upon vitiated intent to transfer (arising from the nondisclosure), or alternatively as parasitic upon the wrong of breach of fiduciary duty. In contrast, the liability to account in Gluckstein is best classified as a claim based solely upon restitution of the wrongdoing. It would be artificial to describe it as a species of subtractive unjust enrichment.

### 7.6 Diversion of Opportunity

The rule of equity which insists on those, who by use of a fiduciary position make a profit, being liable to account for that profit, in no way depends upon fraud, or absence of bonafides; or upon such questions or considerations as whether the profit would or should otherwise have gone to the plaintiff, or whether the profiteer was under a duty to obtain the source of the profit for the plaintiff, or whether he took a risk or acted as he did for the benefit of the plaintiff, or whether he took a risk or acted as he did the benefit of the plaintiff, or whether the plaintiff, has in fact or acted as he did for the benefit by his action. The liability arises from the mere fact of a profit having, in the stated circumstances, been made. The profiteer, however honest and well-intentioned, cannot escape the risk of being called upon to account.

It was clear that the directors could have protected themselves by a resolution of the Legal shareholders approving of their conduct. However, informed consent not having been obtained, they were liable to account.

This was the principle relied upon a *Boardman v. Phipps*,\textsuperscript{13} where the solicitor to a trust and a beneficiary were held liable to account for the profits made as a result of the successful take over and the opportunity of acquiring the shares as a result of acting on behalf of the trustee. It was stated that the transaction required the fully informed consent of both trustees and beneficiaries. These

\textsuperscript{12} (1831) 4 Sim 420, 58 ER 157
\textsuperscript{13} Supra note 5.
extreme applications of the principle are criticized in Jones.

We do not believe that the only function of the civil law should be to compensate and it is our view that restitutionary awards are *prima facie* justified if certain conditions are satisfied. Although the case in favour of restitutionary awards would be strengthened if exemplary damages were abolished, we do not consider that it depends on such abolition.

Our view is that for there to be a restitutionary award the following conditions must be satisfied. First, there must have been either interference with a proprietary right or an analogous right (such as confidentiality and the rights enjoyed by the beneficiary of a fiduciary relationship) or deliberate wrongdoing which could have been restrained by injunction. Secondly, the gains made by the defendant must be attributable to the interest infringed.

In the case of breach of contract we incline to the view that the distinction that appears to be drawn between specifically enforceable contracts and contracts between fiduciaries where a restitutionary award may be made, and other contracts where the gain to a defendant from breach is irrelevant, reflects an appropriate balance of the respective of the parties.