

THE PRINCIPLES OF THE LAW
OF RESTITUTION

The Principles of the Law of Restitution

Second Edition

GRAHAM VIRGO

OXFORD
UNIVERSITY PRESS

OXFORD

UNIVERSITY PRESS

Great Clarendon Street, Oxford OX2 6DP

Oxford University Press is a department of the University of Oxford.
It furthers the University's objective of excellence in research, scholarship,
and education by publishing worldwide in

Oxford New York

Auckland Cape Town Dar es Salaam Hong Kong Karachi
Kuala Lumpur Madrid Melbourne Mexico City Nairobi
New Delhi Shanghai Taipei Toronto

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Argentina Austria Brazil Chile Czech Republic France Greece
Guatemala Hungary Italy Japan Poland Portugal Singapore
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Published in the United States
by Oxford University Press Inc., New York

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First published 2006

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British Library Cataloguing in Publication Data
Data available

Library of Congress Cataloging in Publication Data

Virgo, Graham.

The principles of the law of restitution / Graham Virgo.—2nd ed.
p. cm.

Includes index.

ISBN-13: 978-0-19-928753-6 (hb) : alk. paper

ISBN-13: 978-0-19-929850-1 (pb) : alk. paper 1. Restitution—
Great Britain. 2. Unjust enrichment—Great Britain. I. Title.

II. Title: Restitution.

KD1924.V57 2006

347.41'077—dc22

2006009429

Typeset by Newgen Imaging Systems (P) Ltd., Chennai, India
Printed in Great Britain
on acid-free paper by
Antony Rowe Ltd, Chippenham

ISBN 0-19-928753-8 (Hbk.) 978-0-19-928753-6 (Hbk.)

ISBN 0-19-929850-5 (Pbk.) 978-0-19-929850-1 (Pbk.)

1 3 5 7 9 10 8 6 4 2

For Elizabeth and Jonathan

Preface

The Law of Restitution is like a mountain. From a distance it may appear somewhat insignificant, indeed some have dismissed it simply as a hill, a minor bump on the legal landscape. But on closer inspection, it is definitely a mountain. It is big and complex, and it is very easy to get lost on its slopes. It has been explored many times recently. Some explorers have recorded the mountain's features in great detail. Others have sought to understand how the mountain was formed and why its various features have developed. Others have simply tried to find the safest and quickest routes to the summit. But although many explorers have visited the mountain recently, it has been inhabited for a much longer time. These inhabitants know the mountain well, even though they may not understand all its features, because they work on it every day. They know the quick routes to the summit. The explorers have created new routes, which may be better. But for explorers and inhabitants alike, there is only one true objective: to reach the summit safely. This textbook seeks to provide a map for those who are trying to climb to the top of the mountain. In doing so it attempts to identify the best routes to the summit, where restitutionary remedies can be awarded to the conqueror. But it also seeks to explain the features which are passed on the way and identify the holes and swamps which will catch the unwary. Usually, the route to the summit will be well established and well signposted. Sometimes, however, the most convenient route is one that goes along the byways; along roads which have been forgotten or are rarely used. Occasionally, the map-maker must cut across new country, forging a new route. Maybe others will follow and the authorities may eventually recognize that route as legitimate, as giving those who follow a right of way, but they are unlikely to do so if there is another perfectly serviceable route nearby.

This book owes a great deal to those who have explored the subject before, particularly to the works of Lord Goff, Professor Gareth Jones, Professor Andrew Burrows and the late Professor Peter Birks. It does not seek to describe the law in an encyclopaedic way as Goff and Jones have done in each of the six editions of their seminal work *The Law of Restitution*. Neither does it solely seek to identify a theoretical structure to assist in the organization of the subject, particularly if such a structure has not been expressly recognized in the cases. This is what Birks sought to do in his books *An Introduction to the Law of Restitution* and *Unjust Enrichment*. But none of these works can be characterized as textbooks. The very nature of the law of restitution requires the textbook writer both to describe the law and to identify a coherent and consistent structure which assists in the description and understanding of the subject. As with the previous edition, this book does not seek to concentrate wholly on the theory and policy behind the law,

but seeks to adopt a balance between identification, analysis and justification of the rules themselves and how they operate in practice.

A particular problem for any textbook writer is whether he or she should simply seek to follow the law, by stating it as it is, or seek to lead it on by suggesting the direction in which the law should go. It is both an advantage and a disadvantage of the approach adopted by Birks in particular that he was prepared to lead the judges on. If he was dissatisfied with the analysis adopted in the cases, he was prepared to develop his own analysis and make the cases fit and, if they did not, they were rejected. But sometimes he took this too far and he created theories of restitution which are inconsistent with the cases. A further advantage of the approach adopted by Birks, seen in its purest form in his *Unjust Enrichment*, was that his analysis of the subject was elegant and symmetrical. But the law of restitution is not a work of art; something to be looked at and admired. It is a body of law which must operate in the real world. Elegance and function do not always go together. Far better that the body of law works, even if it has some rough edges. Consequently, some of the conclusions reached in this book lack the elegance of those of Birks, but if they work and, equally importantly, are likely to be recognized and adopted by the judges, the loss of elegance is a small price to pay.

As I have been preparing this edition I have been constantly aware of Peter Birks' profound influence on the development of the subject generally and on my ideas in particular. His penetrating challenges of my approach in the first edition have forced the arguments in this book to become much tighter. Rigour of analysis has been essential. I owe a great debt to Peter for his support, encouragement and interest. His death was a great loss to the law. Whilst in these pages I have expressed disagreement with some of his conclusions, I continue to have the utmost respect for his learning, his approach, and his example.

When the first edition of this book was published I proposed a tripartite structure to the Law of Restitution, whereby restitutionary remedies are triggered by unjust enrichment, wrongdoing, and the vindication of property rights. Subsequent developments in the courts have, for the most part, vindicated this approach. Consequently, the basic structure of this book remains unchanged. But the rapid development of the subject since the first edition was published in 1999 has meant that every chapter has had to be substantially rewritten to take into account new developments and to reflect the currents of the debates amongst commentators and the judiciary. The growing complexity of the subject and rapid expansion of the literature means that the focus on principles is more important to understand this subject than ever before. The tendency in some cases and some writing to advocate an unrestrained discretion in determining the ambit and application of the law of restitution should be resisted. Birks saw the dangers of such a discretionary approach, and he was right.

This book could not have been written without the help and support of many friends and colleagues. My interest in the subject was first triggered at Oxford by Andrew Burrows, Jack Beatson, and John Cartwright. At Cambridge my interest

was nurtured by Gareth Jones. I have had the privilege of teaching *The Law of Restitution* at Cambridge with the best of colleagues and I particularly wish to thank Janet O'Sullivan, Richard Nolan, David Fox, Steve Hedley, Craig Rotherham, Rebecca Williams, and Amy Goymour for their support and assistance. I also want to thank all those students who have helped me formulate my ideas about the subject, often without knowing it. I am also grateful for the support and encouragement of the Fellows and students at Downing College. I wish to express my thanks to the following who have always been willing to answer my questions and from whom I have learned a great deal: Stephen Pitel, Eoin O'Dell, Hang Wu Tang, Jonathan Morgan, Oke Odudu, David Feldman, Edward Burn, Roger Kaye QC, and Clare Stanley. The team at Oxford University Press have been very supportive and helpful and I particularly wish to express my gratitude to Gwen Booth. Finally, the support of my friends and family throughout the period I have been working on this edition is something for which I am most grateful. The Gamlingay Players provided a refuge of normality. The Downing College Tutorial and Admissions Office staff provided assistance in numerous ways. My children, Elizabeth and Jonathan, have brought me down to earth whenever I became obsessed by the subject. My wife, Cally, has remained a constant source of encouragement and strength. To you all, thank you.

I have attempted to state the law as of 19 December, 2005 but it has been possible to incorporate references to some more recent developments.

Graham Virgo

Downing College, Cambridge
19 December 2005

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1

The Essence of Restitution

1. What is the Law of Restitution About?

Before the principles and rules which form the law of restitution are examined it is important to identify what this body of law is actually about. The answer is simple, but it is an answer which has rarely been articulated by judges or commentators. The law of restitution is concerned with the award of a generic group of remedies which arise by operation of law and which have one common function, namely to deprive the defendant of a gain rather than to compensate the claimant for loss suffered.¹ These are called the restitutionary remedies.² Whilst there is a great deal more to the subject than this remedial aspect, since it is also vital to determine what circumstances will trigger the award of restitutionary remedies, it is only because there are a group of remedies which have a common function of depriving defendants of gains that we are able to assert that there is an independent body of law which can be called the law of restitution. To understand what these remedies are, how they operate and when they are available requires examination of a complex body of law. To assist in the understanding of this law it is necessary to identify and analyse the principles which underlie the rules. That is the aim of this book.

2. What is the Nature of Restitutionary Remedies?

(a) The categories of restitutionary remedy

The restitutionary remedies themselves fall into two distinct categories.

(i) *Personal restitutionary remedies*

These are those remedies which restore to the claimant the value of a benefit which the defendant has received. These remedies are said to operate *in personam*.

¹ See Lord Wright of Durley, *Legal Essays and Addresses* (Cambridge: Cambridge University Press, 1939) 36. See also Barker, 'Rescuing Remedialism in Unjust Enrichment Law: Why Remedies are Right' (1998) 57 CLJ 301.

² The range of restitutionary remedies is considered at pp. 21–28 below.

This means that the defendant is liable to pay the value of the benefit to the claimant rather than transfer the benefit itself. Consequently, the claimant has a right against a person, the defendant, rather than a thing, the specific benefit which had been transferred. So, for example, if the claimant pays £1,000 to the defendant by mistake, the defendant will be liable to repay the amount of £1,000 to the claimant even if the defendant no longer has the money which he or she received from the claimant.³ It follows that the award of a personal restitutionary remedy creates a relationship of creditor and debtor between the parties, since the defendant owes money to the claimant. Crucially this category of remedy does not depend on the defendant retaining the benefit which he or she had received from the claimant.

*(ii) Proprietary restitutionary remedies*⁴

The function of these remedies is to enable the claimant to assert his or her property rights in or over an asset which is held by the defendant. These remedies are said to operate *in rem*. There are two types of proprietary restitutionary remedy: first, remedies by virtue of which the claimant can recover the property which is held by the defendant; secondly, remedies which recognize that the claimant has a security interest in property which is held by the defendant. The key advantage of both types of remedy is that, since the claimant has a proprietary interest in an asset which is held by the defendant, the claimant's claim to the asset ranks above other creditors of the defendant, with the result that the claimant is more likely to recover the property or its value if the defendant becomes insolvent. Crucially, this category of remedy does depend on the defendant retaining the property in which the claimant has a proprietary interest.⁵

(b) The characteristics of restitutionary remedies

(i) Restoring what the claimant lost

Since restitutionary remedies are assessed by reference to the defendant's gain, they operate in a very different way from compensatory remedies, where the measure of relief is assessed by reference to the claimant's loss. Despite this, in many cases the effect of a restitutionary remedy will be to restore to the claimant what he or she has lost, because the extent of the defendant's gain will reflect exactly what the claimant lost. 'Restitutionary' is clearly the most appropriate word to describe these remedies, since their function is to restore to the claimant the value of the thing, the thing itself or its substitute which the claimant had lost.

The award of such restitutionary remedies to the claimant can be justified on the ground that, where the defendant has obtained a benefit at the claimant's

³ Subject to the application of defences, such as change of position. See Chapter 24.

⁴ See Chapter 21. ⁵ See Chapter 20.

expense, justice demands that this should be restored to the claimant.⁶ The importance of restitutionary remedies as a mechanism for securing justice between the parties was recognized by Fuller and Perdue:

If, following Aristotle, we regard the purpose of justice as the maintenance of an equilibrium of goods among members of society, the restitution interest presents twice as strong a claim to judicial intervention as the reliance interest, since if A not only causes B to lose one unit but appropriates that unit to himself, the resulting discrepancy between A and B is not one unit but two.⁷

The award of restitutionary remedies consequently operates as a mechanism to secure corrective justice by rectifying an imbalance between the claimant and the defendant.⁸

(ii) *Disgorgement*

In some cases the remedy which is awarded, although it is still assessed by reference to the defendant's gain, results in the claimant obtaining property which he or she never had before. For example, the defendant may have obtained some money from a third party in breach of duty to the claimant. In such circumstances the claimant may be able to make a claim in respect of the money⁹ but, since it has not been taken from the claimant, it is inappropriate to describe the remedy which enables the claimant to obtain this money as literally restitutionary because it is not possible to restore to the claimant what he or she never had in the first place. It is often more appropriate, therefore, to describe the function of such remedies as requiring the defendant to disgorge benefits to the claimant rather than to restore to the claimant what he or she has lost.¹⁰ Even though the description of these remedies as 'restitutionary' is not always felicitous, it is still appropriate to treat them as falling within the law of restitution, simply because the remedy is assessed by reference to a benefit obtained by the defendant.¹¹

Can the award of this type of restitutionary remedy also be justified on the basis that it operates as a mechanism to secure corrective justice between the parties?

⁶ See *Moses v Macferlan* (1760) 2 Burr 1005, 1012; 97 ER 676, 681 (Lord Mansfield) and *Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd* [1943] AC 32, 61 (Lord Wright).

⁷ 'The Reliance Interest in Contract Damages' (1936–37) 46 Yale LJ 52, 56. See Aristotle, 'Nichomachean Ethics', Book V, ch. 2, 4.

⁸ See Barker, 'Understanding the Unjust Enrichment Principle in Private Law: A Study of the Concept and its Reasons' in *Understanding Unjust Enrichment* (ed. Neyers, McInnes and Pitel) (Oxford: Hart Publishing, 2004); Weinrib, *The Idea of Private Law* (London: Harvard University Press, 1995); Smith, 'Restitution: The Heart of Corrective Justice' (2001) 79 Tex. LR 2115. See also *Peel v Canada* (1992) 98 DLR (4th) 140, 165 (McLachlin J).

⁹ See Part IV, below.
¹⁰ Smith, 'The Province of the Law of Restitution' (1992) 71 CBR 672, 696. See also Edelman, *Gain-Based Damages* (2002) (Oxford: Hart Publishing).

¹¹ Birks suggested that the description of these remedies as restitutionary is justified because the 'underlying Latin "*restituere/restitutio*" indicates that the word can include both "give up" and "give back"'. 'Equity in the Modern Law: An Exercise in Taxonomy' (1996) 26 Univ. WALR 1, 28.

The answer is ‘yes’ because the only cases where the defendant will be liable to make restitution to the claimant of benefits which have not been subtracted from the claimant is where the defendant owes duties to the claimant and obtains the benefits in breach of these duties. In other words, the defendant will only be liable to disgorge such benefits where he or she has committed a wrong against the claimant.¹² Justice demands that the defendant should disgorge these benefits because of a fundamental principle of the law of restitution that no defendant should profit from his or her wrongdoing. So disgorgement remedies have a deterrent or distributive function,¹³ but corrective justice also demands that the defendant should disgorge these benefits to the claimant because the claimant is the victim of the wrong and the award of restitutionary relief is a mechanism for protecting the claimant’s rights.¹⁴

3. When will Restitutionary Remedies be Awarded?

Although the policy of corrective justice can be relied on to justify the award of restitutionary remedies, it is too uncertain to operate as an underlying principle on which the law of restitution can be built. For if the question of whether restitutionary remedies could be awarded depended simply on whether it was just to require the defendant to restore what the defendant had gained to the claimant the law of restitution would be unpredictable and unworkable, to such an extent that it would effectively be void for uncertainty. Consequently, it is necessary to identify more specific principles which provide the basis for determining whether the claimant may obtain restitutionary relief. The key question concerns when the law will recognize that the claimant has a right which can be vindicated by means of restitutionary remedies.

Orthodox learning suggests that there is only one principle on which the law of restitution is dependent, namely the principle of unjust enrichment. This is particularly well expressed by Goff and Jones who have said that:

The law of restitution is the law relating to all claims . . . which are founded upon the principle of unjust enrichment.¹⁵

This equation of the law of restitution with the principle of reversing the defendant’s unjust enrichment has been recognized by the judiciary as well. For example, in the case which can be regarded as the source of the modern law of restitution, *Moses v Macferlan*,¹⁶ Lord Mansfield recognized that ‘the gist of this kind of action

¹² See Chapter 15.

¹³ Barker, ‘Understanding the Unjust Enrichment Principle in Private Law: A Study of the Concept and its Reasons’ in *Understanding Unjust Enrichment* (ed. Neyers, McInnes and Pitel), p 101.

¹⁴ Barker, ‘Unjust Enrichment: Containing the Beast’ (1995) 15 OJLS 457, 473.

¹⁵ Goff and Jones, *The Law of Restitution* (6th edn., London: Sweet and Maxwell, 2002) p 3.

¹⁶ (1776) 2 Burr 1005, 1012; 97 ER 976, 981.

is, that the defendant, upon the circumstances of the case, is obliged by the ties of natural justice and equity to refund the money'. Lord Wright, one of the leading proponents of an independent law of restitution, recognized that:¹⁷

It is clear that any civilised system of law is bound to provide remedies for cases of what has been called unjust enrichment or unjust benefit, that is to prevent a man from retaining the money of or some benefit derived from another which it is against conscience that he should keep. Such remedies in English law are generically different from remedies in contract or tort, and are now recognized to fall within a third category of the common law which has been called quasi-contract or restitution.

But it was not until the decisions of the House of Lords, first in *Lipkin Gorman (a firm) v Karpnale Ltd*¹⁸ and then in *Woolwich Equitable Building Society v Inland Revenue Commissioners*¹⁹ that we could be certain that there is a body of law which exists to secure the reversal of unjust enrichment.²⁰ Probably the most important *dictum* of the modern law of restitution is that of Lord Goff in *Lipkin Gorman*, who recognized that:

The recovery of money in restitution is not, as a general rule, a matter of discretion for the court. A claim to recover money at common law is made as a matter of right; and even though the underlying principle of recovery is the principle of unjust enrichment, nevertheless, where recovery is denied, it is denied on the basis of legal principle.²¹

Despite the recognition by the House of Lords that the law of restitution equates with the reversal of the defendant's unjust enrichment, such an interpretation of the law is in fact too simplistic and does not accurately reflect the true operation of the law of restitution.²² For careful analysis of the case law suggests that the law of restitution is not founded upon one principle but rather is founded on three different principles, namely:

- (1) the reversal of unjust enrichment;
- (2) the prevention of a wrongdoer from profiting from his or her wrong; and
- (3) the vindication of property rights with which the defendant has interfered.

¹⁷ *Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd* [1943] AC 32, 61.

¹⁸ [1991] 2 AC 548. See in particular Lord Bridge at p 558, Lord Templeman at p 559 and Lord Goff at p 578.

¹⁹ [1993] AC 70, 197 (Lord Browne-Wilkinson).

²⁰ See also *Westdeutsche Landesbank Girozentrale v Islington London Borough Council* [1996] AC 669, 710 (Lord Browne-Wilkinson), *Kleinwort Benson Ltd v Glasgow CC* [1999] 1 AC 153, 167 (Lord Goff) and 185 (Lord Clyde), *Banque Financière de la Cité v Parc (Battersea) Ltd* [1999] 1 AC 221 and *Kleinwort Benson Ltd v Lincoln CC* [1999] 2 AC 349, 373 (Lord Goff), 406 (Lord Hope). See also *Foskett v McKeown* [2001] 1 AC 102.

²¹ [1991] 2 AC 548, 578.

²² That the law of restitution should not be equated with the unjust enrichment principle was also recognized by Birks: 'Misnomer' in *Restitution: Past, Present and Future* (ed. Cornish, Nolan, O'Sullivan and Virgo) (Oxford: Hart Publishing, 1998) p 7. See also *Unjust Enrichment* (2nd edn Oxford: Oxford University Press, 2005) p 4. For other views on the nature of the law of restitution see, for example, Jackman *The Varieties of Restitution* (Sydney: The Federation Press, 1998) who analyses the law of restitution as involving the reversal of non-voluntary transactions, the fulfilment of non-contractual promises and the protection of facilitative institutions such as property rights and fiduciary relationships.

Restitutionary remedies are available in respect of each of these three principles, but it is vital that they are kept separate and are not brought together within one general principle of unjust enrichment, for the award of restitutionary remedies involves very different considerations depending on which principle the claimant relies. Each of these three principles requires careful description at the outset.

(a) **The reversal of unjust enrichment**

The reversal of the defendant's unjust enrichment is the most important principle in the law of restitution, since it underlies the award of restitutionary relief in a wide variety of cases. It is therefore crucial to determine exactly what unjust enrichment means. Two different senses of the phrase can be identified and it is the failure to distinguish between them which has resulted in the assumption by many that the reversal of unjust enrichment is the only principle on which the award of restitutionary remedies is dependent.

(i) *The descriptive sense of unjust enrichment*

Unjust enrichment may be relied upon simply to describe a state of affairs where the defendant can be said to have been enriched in circumstances of injustice. Since restitutionary remedies will only be awarded where the defendant has received some sort of benefit in circumstances where he or she is required to transfer that benefit or its value to the claimant, this descriptive notion of unjust enrichment can be treated as underlying the whole of the law of restitution. Indeed, it is this idea of unjust enrichment which was recognized by Lord Wright in the *Fibrosa* case²³ and which had earlier been adopted by Lord Mansfield in *Moses v Macferlan*²⁴ where the judges referred to good conscience. This descriptive sense of unjust enrichment has also been recognized by Lord Clyde who said that the unjust enrichment principle 'is equitable in the sense that it seeks to secure a fair and just determination of the rights of the parties concerned in the case'.²⁵

Whilst the award of restitutionary remedies can be justified after the event on the ground that it is just to require the defendant to make restitution, unjust enrichment in this descriptive sense can hardly be considered to be a legal principle which is sufficiently certain to determine when restitutionary remedies should be awarded. Indeed, the assumption in a number of cases that the award of restitutionary remedies was dependent simply on whether or not the defendant had been enriched in circumstances of injustice was one of the main obstacles to the recognition of the law of restitution as an independent body of law. This is illustrated by the *dictum* of Hamilton LJ in *Baylis v Bishop of London*²⁶ that the judges 'are not now free in the

²³ [1943] AC 32, 61. See p 7, above. ²⁴ (1760) 2 Burr 1005, 1012; 97 ER 676, 681.

²⁵ *Banque Financière de la Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 237.

²⁶ [1913] 1 Ch 127, 140. See also *Holt v Markham* [1923] 1 KB 504, 513 where Scrutton LJ described the history of restitution as a 'history of well-meaning sloppiness of thought'.

twentieth century to administer that vague jurisprudence which is sometimes attractively styled “justice as between man and man”.

(ii) *The substantive sense of unjust enrichment*

Alternatively, and much more acceptably, unjust enrichment has been relied on as a substantive principle which can be used to determine in what circumstances restitutionary remedies should be available. To establish this substantive sense of unjust enrichment four questions must be considered:²⁷

- (a) the defendant must have received an enrichment;²⁸
- (b) the enrichment must have been received at the claimant’s expense;²⁹
- (c) the enrichment must have been received in circumstances of injustice, meaning that the claim falls within one of the recognized grounds of restitution;³⁰
- (d) the defendant is not able to rely on a defence which defeats or reduces the claim.³¹

If the first three requirements are satisfied, and the defendant does not have a defence which extinguishes the claim, a restitutionary remedy will be awarded to enable the claimant to recover the value of any enrichment which had been received by the defendant.³² The only remedies which are available for actions founded on the reversal of unjust enrichment are restitutionary remedies and, even then, only personal restitutionary remedies are available.

(b) The deprivation of benefits from a wrongdoer³³

(i) *The nature of restitution for wrongs*

In certain cases the victim of a wrong may be able to bring a restitutionary claim to recover the value of the benefit obtained by the defendant as a result of the wrongdoing. For example, sometimes where the defendant commits a tort against the

²⁷ *Banque Financière de la Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 227 (Lord Steyn). See also *Portman Building Society v Hamlyn Taylor Neck* [1994] 4 All ER 202, 206 (Millett LJ); *Rowe v Vale of White Horse DC* [2003] EWHC 388, [2003] 1 Lloyd’s Rep 418, 421 (Lightman J); *MacDonald v Coys of Kensington* [2004] EWCA Civ 47, [2004] 1 WLR 2775, 2785 (Mance LJ); *Niru Battery Manufacturing Co v Milestone Trading Ltd (No 2)* [2004] EWCA Civ 487, [2004] 2 Lloyd’s Rep 319, paras 28 and 41 (Clarke LJ); *Filby v Mortgage Express (No 2)* [2004] EWCA Civ 759, paras 44–62 (May LJ). Birks, *Unjust Enrichment* (2nd edn.), p. 39 identified a fifth question concerning whether the claimant acquired a personal or a proprietary right. However, the preferable view is that only personal rights are acquired as a result of unjust enrichment, so this is a redundant question.

²⁸ See Chapter 4. ²⁹ See Chapter 5.

³⁰ See Part III. A number of commentators call these grounds of restitution ‘unjust factors’. ‘Grounds of restitution’ is the preferred expression in this book simply for reasons of elegance.

³¹ See Part VI.

³² The determination of the appropriate remedy is sometimes considered to be a fifth question which needs to be examined. See *Lloyds Bank plc v Independent Insurance Co Ltd* [2000] QB 110, 123 (Waller LJ), referring to Millert, ‘Restitution and Constructive Trusts’ in *Restitution: Past, Present and Future* (eds. Cornish, Nolan, O’Sullivan and Virgo), p 208.

³³ See Part IV.

claimant the remedial response is not necessarily assessed by reference to the claimant's loss, but may alternatively be assessed by reference to the defendant's gain.³⁴ A similar response may also arise in respect of benefits accruing to the defendant as a result of a breach of contract,³⁵ the commission of equitable wrongs such as breach of fiduciary duty³⁶ and even the commission of criminal offences.³⁷

Although a number of commentators have argued that the restitutionary response in such circumstances arises because the defendant has been unjustly enriched at the claimant's expense,³⁸ this is only correct to the extent that unjust enrichment is used in its descriptive and not its substantive sense. But where the defendant has received a benefit as a result of the commission of a wrong it is not possible to say that the defendant has been unjustly enriched in any substantive sense for two reasons.³⁹ First, because the claimant's restitutionary claim will succeed even though the defendant's benefit was not obtained directly from the claimant, so it is not possible to show that the defendant has been enriched at the claimant's expense, save in the most artificial sense that the benefit was obtained from the commission of a wrong and the victim was the claimant. Secondly, because it is not necessary to show that the restitutionary claim falls within one of the recognized grounds of restitution. It is sufficient that the defendant has committed a wrong against the claimant and that this wrong is of a type which has been recognized as triggering a restitutionary response. It is this wrongdoing, and not unjust enrichment, which constitutes the cause of action for which the relevant remedy may be restitutionary, although compensatory remedies may also be available.⁴⁰

(ii) The nature of the restitutionary remedy

Where the claimant seeks a restitutionary remedy in respect of a wrong committed by the defendant that remedy will usually be personal. There are, however, cases where the defendant has been awarded a proprietary restitutionary remedy and where the event which triggered this was a wrong.⁴¹ In such cases there is clearly an overlap between the principle of restitution for wrongs and the principle of

³⁴ See Chapter 16.

³⁵ See Chapter 17.

³⁶ See Chapter 18.

³⁷ See Chapter 19.

³⁸ See Burrows, *The Law of Restitution* at pp. 5–6 and the report of the Law Commission, *Aggravated, Exemplary and Restitutionary Damages* (Law Com. No. 247, 1997) p. 51. Birks at one time shared this view (Birks, *An Introduction to the Law of Restitution*, p. 26) but he subsequently changed his mind: 'Misnomer' in *Restitution: Past, Present and Future* (eds Cornish, Nolan, O'Sullivan and Virgo) p. 14.

³⁹ See Smith, 'The Province of the Law of Restitution' (1992) 71 CBR 672, 683.

⁴⁰ Although Burrows stills clings to the quadrature theory, he acknowledges that for restitution for wrongs, the underlying cause of action is the wrong rather than unjust enrichment: *The Law of Restitution* (2nd edn.) at p. 455.

⁴¹ See, for example, *A-G for Hong Kong v Reid* [1994] 1 AC 324 where the Privy Council awarded the claimant a restitutionary proprietary remedy for the defendant's breach of fiduciary duty.

vindicating property rights. It is preferable, however, to treat such claims as ultimately founded on the wrong, since it is the wrong which triggers the recognition of the claimant's proprietary right.⁴²

The justification for the award of restitutionary remedies where the defendant has committed a wrong is the fundamental principle that wrongdoers should not be allowed to profit from their wrongdoing.⁴³

(c) The vindication of property rights with which the defendant has interfered

(i) The nature of restitutionary claims founded on the vindication of property rights

Where the claimant has a proprietary interest in property which has been received by the defendant, whether that proprietary interest previously existed or has been created by operation of law, the claimant will be able to make a claim to obtain a restitutionary remedy to vindicate this proprietary right.⁴⁴ Such proprietary restitutionary claims may take two forms:

(1) Where the defendant received property in which the claimant has a proprietary interest and the defendant has retained that property or its proceeds, the claimant can obtain a proprietary restitutionary remedy in respect of that property itself, the cause of action being the vindication of the claimant's continuing property rights.

(2) Where the defendant received property in which the claimant had a proprietary interest at the time of receipt but that interest has since been lost, the only restitutionary remedy available to the claimant is a personal one, representing the value of the property which the defendant had received. But the cause of action can still be the vindication of property rights, since the claimant can show that the property which the defendant received belonged to the claimant at the time of receipt.

(ii) Is a proprietary restitutionary claim founded on the unjust enrichment principle?

It is often assumed that, where the claimant seeks to recover property in which he or she has a proprietary interest, the recovery of that property or its proceeds can be justified only by reference to the principle that the defendant has been unjustly enriched at the expense of the claimant. But this is only true to the extent that 'unjust enrichment' is used in a trivial, descriptive sense to indicate that the defendant has property which it is just for him or her to return to the claimant.⁴⁵

⁴² *A-G for Hong Kong v Reid* [1994] 1 AC 324. ⁴³ See Chapter 15.

⁴⁴ *Foskett v McKeown* [2001] 1 AC 102, 129 (Lord Millett).

⁴⁵ *Ibid* 115 (Lord Hoffmann).

'Unjust enrichment' in its substantive sense is completely irrelevant in this context because the action to vindicate property rights forms part of the law of property and has nothing to do with the principle of reversing the defendant's unjust enrichment.⁴⁶ Once it has been shown that the defendant has received or has retained property in which the claimant has a proprietary interest then nothing else needs to be proved to establish the claimant's cause of action. If the defendant has the claimant's property he or she should return it, or its value, to the claimant, without the claimant first having to establish that the defendant has been unjustly enriched at his or her expense.

This analysis of proprietary restitutionary claims has now been adopted by the House of Lords in *Foskett v McKeown*.⁴⁷ It remains, however, a controversial analysis and has been criticized by a number of commentators.⁴⁸ For those commentators who argue that unjust enrichment is an adequate explanation of proprietary restitutionary claims, especially to property which is substituted for the original property received, enrichment is readily established because property is generally an enrichment which cannot be subjectively devalued. Further, if the claimant had a proprietary interest in the property or its substitute this shows that the property was received at the claimant's expense. But the stumbling block with this analysis relates to the identification of the ground of restitution. Some commentators are forced to identify artificial grounds of restitution to explain the decided cases. But such artifice is completely unnecessary. The reported cases do not use such reasoning and they have no need to do so, simply because it is sufficient to establish that the defendant has received property in which the claimant has a proprietary interest.

Before the decision of the House of Lords in *Foskett v McKeown* a number of cases were consistent with the theory that proprietary restitutionary claims are not founded on unjust enrichment. For example, in *Macmillan v Bishopsgate Investment Trust plc (No 3)*⁴⁹ the claimant wished to recover shares from the defendants which had been transferred to them by a third party in breach of trust. The defendants pleaded the defence that they were *bona fide* purchasers for value.⁵⁰ The issue before the court concerned the choice of law rule for this type of restitutionary action. It was agreed that the claimant's claim should be characterized as restitutionary and the argument then related to whether this claim was based on an obligation or property. The Court of Appeal unanimously held that it was a matter of

⁴⁶ See Chapter 20. See also Grantham and Rickett, 'Property and Unjust Enrichment: Categorical Truths or Unnecessary Complexity?' [1997] 2 NZ Law Rev. 623 and Hedley, *Restitution: Its Division and Ordering* (London: Sweet and Maxwell, 2001), p 150.

⁴⁷ [2001] AC 102.
⁴⁸ See especially Birks, *Unjust Enrichment* (2nd edn), pp. 34–36; Burrows, 'Proprietary Restitution: Unmasking Unjust Enrichment' (2001) 117 LQR 412 and Smith, *The Law of Tracing*, (Oxford: Clarendon Press, 1997), p 300.

⁴⁹ [1996] 1 WLR 387. See Virgo, 'Reconstructing the Law of Restitution' (1996) 10 TLI 20 and Swadling, 'A Claim in Restitution?' [1996] 1 LMCLQ 63 for further discussion of this case.

⁵⁰ See Chapter 22.

property and so proprietary choice of law rules were applicable. The importance of this case is that the court implicitly recognized that a cause of action could be restitutionary even though the action was not founded upon the reversal of an unjust enrichment. For example, Auld LJ emphasized that the issue in the case was essentially a proprietary one and stated that ‘it is difficult to see what unjust enrichment the [defendants] have had’.⁵¹ Further, the result, but not the analysis, of the leading case of *Lipkin Gorman (a firm) v Karpnale Ltd*⁵² is consistent with the proprietary restitutionary claims theory. Although the House of Lords, following the lead of Lord Goff, agreed that all restitutionary claims are founded on the unjust enrichment principle, this is not in fact an unjust enrichment case, save in the broadest and least useful descriptive sense of the defendant having received a benefit which should be returned as a matter of justice. Rather, *Lipkin Gorman* was a case which was primarily concerned with the vindication of the claimant’s proprietary rights. This explains why none of the judges expressly identified all of the elements which are required to establish that the defendant has been unjustly enriched, most notably the ground for restitution, an omission which has been a serious cause of concern for some commentators.⁵³ This is not a problem if the basis for awarding restitutionary remedies was the vindication of property rights rather than the reversal of unjust enrichment, because where the claimant wishes to vindicate property rights it is only necessary to identify the property right and not a ground of restitution.

Lipkin Gorman v Karpnale concerned a partner of the claimant firm of solicitors who had stolen money from the firm over a period of time and used this money to gamble at the defendant’s casino. The claimant brought a restitutionary claim against the defendant to recover the value of the money received by the defendant. The claimant’s action succeeded. Both Lords Templeman and Goff emphasized the claimant’s continuing proprietary interest in the money from the moment it was stolen by the partner until it, or its substitute, was received by the defendant.⁵⁴ Consequently, a continuing proprietary interest was clearly recognized and appears to have proved vital to the success of the claim. If this analysis is correct we are left with a nice irony. Whilst the decision of the House of Lords in *Lipkin Gorman v Karpnale* is of prime importance as the leading case where the unjust enrichment principle was accepted as forming part of English law, that case is not itself authority for the application of the unjust enrichment principle on the facts.

That this is the proper conclusion has now been confirmed by the decision of the House of Lords in *Foskett v McKeown*,⁵⁵ where the majority recognized

⁵¹ [1996] 1 WLR 387, 409. ⁵² [1991] 2 AC 548.

⁵³ See Birks, ‘The English Recognition of Unjust Enrichment’ [1991] LMCLQ 473, McKendrick, ‘Restitution, Misdirected Funds and Change of Position’ (1992) 55 MLR 377 and Burrows, *The Law of Restitution* pp 191–193. These commentators consider that the ground of restitution was that of ignorance, even though none of the judges referred to any such ground of restitution. See Chapter 7 for further discussion of ignorance as a ground of restitution.

⁵⁴ [1991] 2 AC 548, 560 (Lord Templeman), 572 (Lord Goff). ⁵⁵ [2001] AC 102.

a fundamental distinction between the law of unjust enrichment and the law of property and held that a claim to recover substitute property in which the claimant asserted an equitable proprietary interest depended on the vindication of property rights and not unjust enrichment. *Foskett v McKeown* concerned a claim brought by the beneficiaries of a trust to recover part of the proceeds of a life insurance policy. One of the trustees had misappropriated money from the trust fund to pay at least the fourth and fifth annual premiums for a life assurance policy, with the earlier premiums being paid from his own money.⁵⁶ After the fifth premium of £10,220 had been paid the trustee committed suicide and his children were entitled to receive a payment of just over £1 million under the policy. The beneficiaries of the trust claimed a proportionate share of this sum, amounting to £400,000, on the basis that trust money had been used to pay two of the premiums which contributed to the receipt of the death benefit by the children. The Court of Appeal⁵⁷ had confined the beneficiaries to a lien on the proceeds of the policy to secure payment of the amount which had been misappropriated from the trust, amounting to £20,440. The House of Lords held by a bare majority that the beneficiaries' claim for a proportionate share should succeed. The importance of the decision for present purposes is the recognition that the restitutionary claim of the beneficiaries fell within the law of property and was concerned with the vindication of property rights rather than with whether the defendant was unjustly enriched at the expense of the claimant.⁵⁸

Almost as important was the clear rejection by most of the judges of a normative approach to proprietary restitutionary claims, by virtue of which the identification and vindication of proprietary rights would depend on the discretion of the court. This rejection was forcefully expressed by Lord Millett:⁵⁹

Property rights are determined by fixed rules and settled principles. They are not discretionary. They do not depend upon ideas of what is 'fair, just and reasonable.' Such concepts, which in reality mask decisions of legal policy, have no place in the law of property.⁶⁰

Lord Browne-Wilkinson also recognized that proprietary claims do not depend on any discretion vested in the court; it was 'a case of hard-nosed property rights'.⁶¹ The approach of the court could not have been clearer: where the claimant is seeking a proprietary restitutionary remedy the claim is founded on the claimant's rights in the property held by the defendant rather than the defendant's unjust enrichment.

⁵⁶ Although it was unclear whether the third premium was paid from the trustee's own money or from the trust fund. ⁵⁷ [1998] Ch 265.

⁵⁸ [2001] 1 AC 102, 109 (Lord Browne-Wilkinson), 115 (Lord Hoffmann), 118 (Lord Hope) and 129 (Lord Millett). Lord Steyn concluded that the children were not unjustly enriched because the payment of the premiums did not constitute an enrichment: *ibid* 112. ⁵⁹ *Ibid* 127.

⁶⁰ *Cp.* Lord Hope who said, *ibid* at 120, that since there was no principle or authority to assist with the division of the mixed substitution in this case it should be divided in such proportions as were equitable, having regard to the terms of the life insurance policy and the equities affecting each party. ⁶¹ *Ibid* 109.

(iii) Criticisms of the vindication of proprietary rights principle

The recognition of a vindication of proprietary rights principle as distinct from an unjust enrichment principle has been criticized on three grounds:

(1) One criticism of the vindication of property rights principle is that, whereas unjust enrichment is an event for which restitutionary remedies are available, it is not possible to treat proprietary rights as an event and so it is not possible to contrast unjust enrichment and property rights as triggers of restitutionary remedies.⁶² This argument stems from the writings of Birks who drew a fundamental distinction⁶³ between events and responses. According to Birks, in the law of civil obligations it is necessary to identify an event before the appropriate response can be considered. The law, he asserted, recognizes four events, namely consent, wrongs, unjust enrichment and other events. Where the event of unjust enrichment can be established the only response is restitution. Vindication of property rights is not an event and so, he concluded, restitution cannot respond to it. As he said:

The key point is that the law of property is not formed in answer to a question about causative events: 'How do rights arise?' It is formed in response to the quite different question: 'Against whom are rights exigible?'⁶⁴

He concluded that:

It is an error of logic to force a choice between the law of property and the law of unjust enrichment.

But this choice between the law of property and the law of unjust enrichment is not the relevant choice which should be made. The use of the phrase 'property rights' is neutral and does not suggest that any event has occurred. But the crucial feature of the vindication of property rights principle is that the defendant has interfered with the claimant's property rights by not allowing the claimant the exclusive benefit of his or her rights. It is this interference which justifies the award of restitutionary remedies and which can be analysed as the appropriate event.⁶⁵

(2) A second related criticism is that unjust enrichment and the vindication of property rights cannot be considered to be distinct principles since the claimant's property right might be created because the defendant was unjustly enriched at

⁶² Birks, *Unjust Enrichment* (2nd edn.), p 33; Burrows, 'Proprietary Restitution: Unmasking Unjust Enrichment' (2001) 117 LQR 412. In *Kuwait Airways Corp v Iraqi Airways Co (Nos 4 and 5)* [2002] UKHL 19, [2002] 2 AC 883, 1093 Lord Nicholls of Birkenhead, in the context of the tort of conversion, characterized the vindication of the claimant's property rights as involving unjust enrichment.

⁶³ See especially 'Equity in the Modern Law: An Exercise in Taxonomy' (1996) 26 Univ. WALR 1, 8–10; 'Property, Unjust Enrichment and Tracing' [2001] CLP 231. ⁶⁴ *Ibid* 241.

⁶⁵ See Grantham and Rickett, 'Property and Unjust Enrichment: Categorical Truths or Unnecessary Complexity?' [1997] NZ Law Rev. 668, 680; Grantham and Rickett, 'Property Rights as a Legally Significant Event' (2003) CLJ 717.

the claimant's expense. This was particularly the view of Birks⁶⁶ who argued that both personal and proprietary rights might be triggered as a response to unjust enrichment. But no case has expressly recognized that property rights might arise simply because the defendant has been unjustly enriched at the claimant's expense. Birks⁶⁷ considered that *Foskett v McKeown*⁶⁸ was such a case, even though the majority judgments clearly contradict this, and that there are other cases which are consistent with this approach, including *Sinclair v Brougham*,⁶⁹ but this has been overruled,⁷⁰ and *Chase Manhattan Bank v Israel-British Bank*,⁷¹ but this case was subsequently re-interpreted by the House of Lords.⁷² Further, none of these cases explicitly recognizes that property rights can derive from unjust enrichment. There is simply no empirical evidence to support the assertion that property rights can derive from the defendant's unjust enrichment. Also, there is no need to rely on the substantive unjust enrichment principle to explain why the claimant has a proprietary interest in property. It is sufficient that the claimant's case falls within one of the recognized categories of case by virtue of which property rights arise and none of these cases requires the claimant to establish specifically that the defendant has been unjustly enriched at the expense of the claimant.⁷³ It follows that the substantive unjust enrichment principle should be considered as triggering only personal and not proprietary rights.

(3) A final criticism of the vindication of property rights principle is the use of the word 'vindication'. Certainly, the use of the word can be criticized on the technical ground that vindication refers to a specific remedy by virtue of which property, which is in the possession of the defendant but belongs to the claimant, is restored to the claimant. This *vindicatio* is not recognized at common law and even in equity it is not the only remedy where the defendant has interfered with the claimant's property rights,⁷⁴ so it could be concluded that it is not appropriate to refer to the vindication of property rights, since property rights are not necessarily vindicated. Nevertheless, the use of the word 'vindication' does serve a useful function. This is because it describes, albeit in general terms, the nature of the remedies where property rights have been interfered with by the defendant. The word 'vindication' relates to the phrase 'property rights' in the same way that the word 'reversal' relates to 'unjust enrichment'.⁷⁵ Because of the technical meaning of vindication an alternative word could be suggested, such as 'protection', but this too lacks precision since it suggests that the restitutionary remedy will be awarded before the proprietary right has been interfered with, to ensure that such

⁶⁶ *Unjust Enrichment* (2nd edn.), p 33; 'Misnomer' in *Restitution: Past, Present and Future* (ed. Cornish, Nolan, O'Sullivan and Virgo).

⁶⁷ *Unjust Enrichment* (2nd edn.), p 35.

⁶⁸ [2001] 1 AC 102.

⁶⁹ [1914] AC 398.

⁷⁰ *Westdeutsche Landesbank Girozentrale v Islington LBC* [1996] AC 669. See p 612, below.

⁷¹ [1981] Ch 105.

⁷² *Westdeutsche Landesbank Girozentrale v Islington LBC* [1996] AC 669. See p 608, below.

⁷³ See Chapter 20.

⁷⁴ See Chapter 21.

⁷⁵ The equivalent word for wrongdoing is the not very useful 'remedy'.

interference does not occur, whereas typically the property right has already been interfered with, hence the need for a restitutionary remedy. Consequently, the word 'vindication' will be used in this book, as the most useful word, albeit not the most accurate, to describe the award of restitutionary remedies where the defendant has interfered with the claimant's property rights.⁷⁶

(iv) Justifying the award of restitutionary remedies to vindicate property rights

The justification for the award of restitutionary remedies to vindicate the claimant's property rights stems from the fundamental principle of English law that property rights are of such importance that they are deserving of particular protection.⁷⁷ But, despite this, it might be thought that it does not matter whether the restitutionary claim is analysed with reference to the vindication of property rights or unjust enrichment. It is certainly true that in many cases the same result will be achieved regardless of how the claim is analysed. But the proper analysis can matter for practical reasons, such as whether the defence of change of position should apply,⁷⁸ what the elements of the respective causes of action might be and which remedies are potentially applicable. It also matters for intellectual reasons, since it is the legitimacy of the vindication of property rights principle which has become the battleground for vital theoretical discussion amongst commentators and increasingly judges about the proper classification of rights and remedies both at law and in equity.

(d) Summary of the key principles

The consequence of the analysis adopted in this book and the recent developments in the courts is that the law of restitution should properly be analysed in the following way. The law of restitution is concerned with all claims where the remedy which the claimant seeks is a restitutionary remedy which is assessed with reference to the defendant's gain. Restitutionary remedies are available in three situations: first, where it can be shown that the defendant has been unjustly enriched—here the only remedies which are available are personal restitutionary remedies; secondly, where the defendant has committed a wrong for which restitutionary relief may be available—here the remedy may be restitutionary but it can also be compensatory; finally, where the claimant wishes to vindicate his or her property rights—here the remedy is typically restitutionary and, depending on whether or not the defendant retains property in which the

⁷⁶ The use of the word 'vindication' does have some judicial support: see, for example, *Tinsley v Milligan* [1994] 1 AC 340, 368 (Lord Lowry) and *Foskett v McKeown* [2001] AC 102, 129 (Lord Millett).

⁷⁸ See Chapter 24.

⁷⁷ See Chapter 20.

claimant has a proprietary interest, the restitutionary remedy will either be proprietary or personal.

4. What is the Justification for Recognizing an Independent Law of Restitution?

When the law of restitution was equated with the law of unjust enrichment the justification for recognizing an independent body of law called the law of restitution was clear, since it was a distinct subject different from contract, tort and the law of property. But once it is accepted that the law of restitution is not confined to the law of unjust enrichment, but is simply a body of law concerning the types of remedy which may be awarded in particular circumstances, the justification for recognizing an independent law of restitution is more difficult to find. It might be thought better to stop talking about and studying the law of restitution and instead concentrate our efforts on the law of unjust enrichment⁷⁹ and, where relevant, wrongdoing and vindication of proprietary rights. This would be a mistake.

The main reason for identifying any legal category, such as contract, equity or company law, is that, by grouping cases together which are concerned with the same legal issues, common principles can be identified which assist in the better understanding and prediction of the law. This is true of the law of restitution as well. There are a number of common principles and questions of policy which underlie all restitutionary claims regardless of the cause of action.⁸⁰ So, for example, there are important questions of relevance to all restitutionary claims concerning how restitutionary remedies should be assessed. Similarly, there are defences and bars which are generally applicable to all restitutionary claims regardless of the principle on which that claim is founded. Also, as a mechanism for analysis of the law, the law of restitution remains a useful hook on which to hang disparate areas of law. It forces us to make connections which might otherwise be ignored and so the subject remains of great use for the purposes of exposition. So, for example, when considering the role of fault,⁸¹ the way fault is interpreted in one part of the law of restitution will be of importance when considering the issue in another area.⁸² For all of these reasons much is to be gained by recognizing the law of restitution as an independent body of law in its own right, where the only common characteristic is that it concerns the award of remedies which are assessed by reference to the benefit obtained by the defendant.

⁷⁹ As Birks did in *Unjust Enrichment*.

⁸⁰ These are identified and examined in Chapter 2.

⁸¹ See p 37, below.

⁸² See Virgo, 'The Role of Fault in the Law of Restitution' in *Mapping the Law of Obligations* (ed. Burrows) (Oxford: Oxford University Press, 2006).

5. The Obstacles of History

Although this book is not the place for a detailed examination of the history of the law of restitution,⁸³ the essential features of that history remain of vital importance to a proper understanding of the modern subject, particularly because this explains why an independent law of restitution was only recently fully recognized by the House of Lords in *Lipkin Gorman (a firm) v Karpnale Ltd.*⁸⁴

(a) The implied contract theory

The law of restitution had its origins in the old forms of action, particularly the action of *indebitatus assumpsit* which was developed in the seventeenth century. The function of this action was to enable the claimant to recover a sum of money from the defendant after the claimant had established that the defendant owed a debt to the claimant which the defendant had promised to repay. Although the essential feature of the action was that a debt was owed by the defendant, the promise of repayment was required to enable the action to be accommodated within the system of formal pleading which existed at the time. Although initially the defendant's promise to repay the claimant had to be proved expressly, increasingly it was implied from the circumstances of the case, so that the promise became a fiction.⁸⁵ This was recognized by Barry J in *William Lacey (Hounslow) Ltd v Davis*⁸⁶ who said:

In these quasi-contractual cases the court will look at the true facts and ascertain from them whether or not a promise to pay should be implied, irrespective of the actual views or intentions of the parties at the time when the work was done or the services rendered.

In fact the award of restitution in these cases can, in retrospect, be justified by reference to the principle of unjust enrichment. But, until the middle of the twentieth century, the claim depended on whether it was possible to imply a promise by the defendant to repay the claimant. If the facts of the case were inconsistent with the implication of such a promise it followed that the claimant's restitutionary claim must fail. So, for example, restitutionary remedies could not be awarded where there was an express contract in existence which prevented a contract from being implied or where one of the parties was incapacitated from making a contract.

⁸³ For detailed analysis of the history of restitution see Jackson's *The History of Quasi-Contract in English Law* (Cambridge: Cambridge University Press, 1936). See also Baker, 'The History of Quasi-Contract in English Law' in *Restitution: Past, Present and Future* (ed. Cornish, Nolan, O'Sullivan and Virgo) Chapter 3 and Ibbetson, *A Historical Introduction to the Law of Obligations* (Oxford: Clarendon Press, 1999) Part IV.

⁸⁴ See *Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd* [1943] AC 32, 63 (Lord Wright).
⁸⁶ [1957] 1 WLR 932, 936.

(b) Rejection of the implied contract theory

It was this emphasis on promise and the notion of an implied contract that proved to be the main obstacle to the recognition of an independent law of restitution. For analysis in terms of implied promises meant that the question whether a restitutionary remedy was available was treated simply as an appendix to the law of contract, as was reflected by the fact that such restitutionary liability was characterized as quasi-contractual.⁸⁷ The law of restitution has, however, been emancipated from its reliance on contract. This occurred in the important case of *United Australia Ltd v Barclays Bank Ltd*⁸⁸ where Lord Atkin memorably said:

These fantastic resemblances of contracts invented in order to meet requirements of the law as to forms of action which have now disappeared should not in these days be allowed to affect actual rights. When these ghosts of the past stand in the path of justice clanking their medieval chains the proper course for the judge is to pass through them undeterred.⁸⁹

It follows that restitutionary claims will succeed even though it is not possible to imply a contract between the parties. But this rejection of the implied contract theory as the principle which underlies the award of restitutionary remedies does not prevent a claimant from suing the defendant on an implied contract. The effect of the *United Australia* case is to remove the fiction of an implied contract from English law, but it does not prevent the implication of a contract from the facts where the evidence is consistent with such an implication. Where, however, there is insufficient evidence to imply a contract, relief can still be obtained by operation of law, by reference to principles such as unjust enrichment.⁹⁰

(c) The legacy of the implied contract theory

The legacy of the fictional implied contract does unfortunately live on since judges still sometimes consider whether a contract can be implied when determining whether restitutionary relief should be available to the claimant. One of the most blatant modern examples of such reliance on the implied contract principle is contained in the judgment of Millett LJ in *Taylor v Bhail*.⁹¹ One of the questions for the court in that case was whether a builder could recover the reasonable value of his building work from a customer after the builder had inflated the estimated price of the work to enable the customer to defraud his insurance company. This inflation of the price made the transaction illegal and, since the courts will not enforce illegal transactions,⁹² the claimant's action on the contract failed.

⁸⁷ An expression which had been recognized by Lord Mansfield in *Moses v Macferlan* (1760) 2 Burr 1005, 1008; 97 ER 976, 978.

⁸⁹ *Ibid* 28. ⁹⁰ Cp. Hedley, 'Implied Contract and Restitution' (2004) CLJ 435.

⁹¹ [1996] CLC 377. See also *Guinness plc v Saunders* [1990] 2 AC 663, 689 (Lord Templeman).

⁹² *Holman v Johnson* (1775) 1 Cowp 341; 98 ER 1120. See Chapter 26.

But Millett LJ also concluded that the claimant's restitutionary claim should fail because:

The illegality renders any implied promise to pay a reasonable sum unenforceable—just as it renders the express promise to pay the contract price unenforceable.

Such reliance on quasi-contractual reasoning should have no part to play in the modern law of restitution. The obligation to make restitution is imposed as a matter of law and does not involve enforcement of any fictional promise made by the defendant.⁹³

6. The Principal Types of Restitutionary Remedy

There are a number of different restitutionary remedies which will be examined throughout this book. At this stage it is sufficient to identify the most important ones. Whilst the remedy which is available for a particular restitutionary claim will vary according to the circumstances of the case, the function of all restitutionary remedies is 'to effect a fair and just balance between the rights and interests of the parties concerned'.⁹⁴

(a) Money had and received

Although money had and received was one of the common counts which is still referred to today when pleading a restitutionary claim, it is more appropriate to treat money had and received as a restitutionary remedy rather than a cause of action. This is a common law restitutionary remedy which is applicable where the claimant simply wishes to recover money which had been paid to the defendant. It is a personal remedy which exists only at common law and enables the claimant to recover the value of the money received by the defendant rather than the actual notes and coins.

(b) Reasonable value of property and services

Where the claimant has transferred property to the defendant or has provided a service for the benefit of the defendant and the claimant successfully brings a restitutionary claim in respect of these benefits, the typical remedy which he or she will be awarded is a financial one, assessed by reference to the value of the benefit received by the defendant. Where the claim is for the reasonable value of the property transferred this is called a *quantum valebat*, and where the claim is for the

⁹³ This view has been endorsed in the House of Lords in *Westdeutsche Landesbank Girozentrale v Islington London Borough Council* [1996] 2 AC 669, 710 (Lord Browne-Wilkinson).

⁹⁴ *Banque Financière de la Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 237 (Lord Clyde).

reasonable value of services this is called a *quantum meruit*. The question of valuation of goods and particularly services is one which is fraught with difficulty.⁹⁵

(c) Account of profits⁹⁶

Where the defendant has committed a wrong against the claimant, such as a breach of fiduciary duty, and the defendant makes a profit as a result, one of the restitutionary remedies which may be awarded is that of an account of profits. This involves an account being taken to ascertain the profit made by the defendant as a result of the wrongdoing, which the defendant is then liable to pay to the claimant. This is a personal remedy, since the defendant is only required to transfer the value of the profit made.⁹⁷

(d) Restitutionary damages⁹⁸

Whereas an account of profits can only be awarded where the defendant has profited from the commission of a wrong, there may be circumstances where the defendant has benefited from wrongdoing by saving expenditure and it is appropriate to deprive the defendant of this benefit by means of a restitutionary remedy. An appropriate name for this remedy is 'restitutionary damages'. However, in *Attorney-General v Blake*⁹⁹ Lord Nicholls rejected this title in favour of account of profits. It appears that the reason for this rejection was because of a sense that the word 'damages' only relates to a compensatory remedy which arises where the claimant has suffered a loss as a result of the commission of a wrong. Now it is true that damages usually does have a compensatory connotation, but if the prefix 'restitutionary' is used then there is no obvious objection to the name of this remedy and it is clear that this type of remedy does need to be recognized to deal with the situation where the benefit obtained by the defendant involves money saved rather than profit gained. Consequently, the term 'restitutionary damages' will be used in this book, but only to name the remedy concerned with restitution of a negative benefit, and account of profits will be used where the defendant has obtained a positive benefit as a result of the commission of a wrong.

The term 'restitutionary damages' is also being used increasingly in another sense, to reflect the remedy which is awarded where a wrongdoer has obtained a profit at the expense of the claimant. Edelman in particular has argued that in such circumstances the appropriate remedy is properly described as restitutionary, since it restores to the claimant what the defendant had gained.¹⁰⁰ He considers

⁹⁵ See Chapter 4. ⁹⁶ See Chapter 15.

⁹⁷ The profit may, however, be held on constructive trust so that the claimant has an equitable proprietary interest in the profit. See Chapter 18.

⁹⁸ See Chapter 15 and *Aggravated, Exemplary and Restitutionary Damages* (Law Com. No. 247, 1997) p 51.

⁹⁹ [2001] 1 AC 268.

¹⁰⁰ Edelman, *Gain-Based Damages* (Oxford: Hart Publishing, 2002) p 66.

that many of the cases where an account of profits was ordered are not restitutionary as such, but involve disgorgement of a benefit where the benefit arose from the commission of a wrong against the claimant but the benefit did not come from the claimant. This is an important distinction, which is examined in Chapter 15. However, the names of the remedies themselves are a cause for confusion. For even a disgorgement remedy can be described as restitutionary as used in this book, since it is a gain-based remedy, and it is still necessary to identify a remedy which will apply where a defendant has saved money rather than made a profit. Consequently, it is preferable to describe the usual remedies for wrongdoing as involving either account of profits, where the wrongdoer obtained an actual profit from the wrong, or restitutionary damages, where money was saved.

(e) Recognition of a beneficial interest

Where the defendant has received and retains property in which the claimant has a continuing equitable proprietary interest, the defendant may be required to hold that property on trust for the claimant.¹⁰¹ This means that the claimant can call for the return of the property whenever he or she wishes.¹⁰² This type of proprietary restitutionary remedy involving the transfer of property is not available at common law. Consequently, if the defendant has property in which the claimant has retained a legal proprietary interest the claimant is only able to obtain the value of the property and is not able to recover the property itself.

(f) Equitable charge¹⁰³

Where the defendant has property in which the claimant has an equitable proprietary interest an alternative restitutionary remedy to that of recognizing that the claimant has a beneficial interest in the property is for the courts to impose an equitable charge over it. This is a proprietary restitutionary remedy since it recognizes that the claimant has a proprietary interest in the property to secure repayment of what the defendant owes to the claimant. Consequently, the claimant cannot compel the defendant to transfer the property to him or her, but the claim for repayment is given priority over unsecured creditors of the defendant.

(g) Subrogation¹⁰⁴

Subrogation is a restitutionary remedy which is designed to ensure 'a transfer of rights from one person to another . . . by operation of law'.¹⁰⁵ Essentially the

¹⁰¹ See Chapter 21.

¹⁰² See *Saunders v Vautier* (1841) 4 Beav 115; 49 ER 282.

¹⁰³ See Chapter 21.

¹⁰⁴ See Mitchell, *The Law of Subrogation* (Oxford: Clarendon Press, 1995).

¹⁰⁵ *Orakpo v Manson Investments Ltd* [1978] AC 95, 104 (Lord Diplock).

function of subrogation is to enable the claimant to rely on the rights of a third party against a defendant, or the rights of a defendant against a third party. This will be a particularly useful remedy where, for example, the claimant lends money to the defendant in circumstances where the claimant thinks that the loan is secured by a charge so that he or she has priority over the defendant's other creditors. If the charge is invalid the claimant would simply be an unsecured creditor and so will not have priority over other creditors. In such a case the claimant could be subrogated to the rights of another secured creditor of the defendant, even though that security had been discharged. The security in such circumstances is treated as though it had been assigned to the claimant,¹⁰⁶ so that he or she is able to rely on it as against the defendant and so gain priority over the defendant's unsecured creditors. Since subrogation is a restitutionary remedy, this notional assignment of the charge is only effective as against a defendant who is liable to make restitution to the claimant.

In the leading case of *Banque Financière de la Cité v Parc (Battersea) Ltd*¹⁰⁷ the House of Lords recognized that there are two forms of subrogation which are recognized in English law.

(i) Contractual

The first type is that which arises by virtue of the express or implied intentions of the parties, as occurs in contracts of insurance where a term is implied that insurers are subrogated to the rights of the assured against the party who caused loss.¹⁰⁸ Since this right to subrogation arises by virtue of contract, it has nothing to do with the law of restitution.¹⁰⁹

(ii) Restitutionary

The other type of subrogation is the equitable remedy which is available by operation of law as a restitutionary remedy specifically to reverse the defendant's unjust enrichment.¹¹⁰ It may also be used to *prevent* the defendant's unjust enrichment.¹¹¹ Although the matter was not discussed by the House of Lords, subrogation will also be available where the claimant's restitutionary claim is founded on the vindication of proprietary rights, and is in fact most likely to arise in such circumstances.¹¹² Whilst the remedy is in principle available where the claim is founded on the commission of a wrong, there are no cases where such a remedy has been awarded and it is difficult to conceive of a case where such a remedy would be appropriate.

¹⁰⁶ *Banque Financière de la Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 236 (Lord Hoffmann).

¹⁰⁷ [1999] 1 AC 221.

¹⁰⁸ See, for example, *Lord Napier and Ettrick v Hunter* [1993] AC 713.

¹⁰⁹ *Hobbs v Marlowe* [1978] AC 16, 39 (Lord Diplock).

¹¹⁰ *Banque Financière de la Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 231 (Lord Hoffmann); *Filby v Mortgage Express (No 2) Ltd* [2004] EWCA Civ 759.

¹¹¹ *Banque Financière de la Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 231 (Lord Hoffmann).

¹¹² *Halifax plc v Omar* [2002] EWCA Civ 21, [2002] 2 P and CR 377; *Eagle Star Insurance Co Ltd v Karasiewicz* [2002] EWCA Civ 940. See Chapter 21.

The function of the remedy of subrogation is illustrated by the facts of the *Banque Financière* case itself. In that case the claimant had lent a sum of money to the debtor company, which used the money to pay off part of a debt owed by it to a third party, this debt having been secured by a charge over property. The defendant company, which was in the same group as the debtor, had a second charge over the same property. When the claimant lent the money to the debtor company the claimant received a letter of postponement which stated that the claimant's debt would be paid off in priority to any other company in the group. Clearly the intention behind this letter was to give the claimant priority over the defendant, but it was ineffective to give the claimant priority as a matter of law. The debtor company became insolvent and the question for the House of Lords to resolve was whether the debt which that company owed to the claimant should be discharged before that which was owed to the defendant. The court concluded that the defendant had been unjustly enriched at the expense of the claimant. The defendant was enriched at the claimant's expense because the claimant's money was used partially to discharge the liability of the third party, and this improved the chances of the defendant being repaid. This enrichment was unjust because the claimant had mistakenly believed that the effect of the letter of postponement was that it had priority over the defendant and, had it not made this mistake, it would not have lent the money in the first place.¹¹³ The court concluded that the most appropriate remedy to reverse the defendant's unjust enrichment was to subrogate the claimant to the rights of the third party against the debtor company. This meant that, as between the claimant and the defendant, the claimant had the benefit of the third party's charge so that the claimant obtained priority over the defendant. The particularly important feature of the remedy of subrogation in this case was that it operated as a personal remedy, since the claimant only obtained priority over the defendant and not as regards any of the other creditors of the debtor company.¹¹⁴ In other circumstances it might be appropriate to treat the remedy of subrogation as having proprietary consequences, by giving the claimant priority over other creditors of the debtor.¹¹⁵

(h) The award of interest

Since it is a function of restitutionary remedies that the defendant should be deprived of those gains obtained as a result of being unjustly enriched, having committed a wrong or receiving property in which the claimant has a proprietary interest, it should follow automatically that whenever pecuniary restitutionary remedies are awarded the claimant should also be awarded interest. This is because, immediately the defendant has received a benefit which he or she is liable

¹¹³ See Chapter 8 for examination of mistake as a ground of restitution.

¹¹⁴ *Banque Financière de la Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 228 (Lord Steyn) and 237 (Lord Clyde). See also *Filby v Mortgage Express (No 2) Ltd* [2004] EWCA Civ 759.

¹¹⁵ See Chapter 21.

to restore to the claimant, the defendant is not entitled to the benefit and so should pay the claimant for its use. The law of restitution accepts this argument, and so the defendant is liable to pay the claimant for the use of the benefit by means of the award of interest.

But when it comes to assessing the interest which the defendant is liable to pay to the claimant the law becomes much more controversial. Should simple or compound interest be awarded? Simple interest may be awarded by virtue of s 35A of the Supreme Court Act 1981. It is awarded on the amount of money which is owed by the defendant to the claimant. Compound interest has traditionally been awarded in equity where money has been obtained or retained by fraud or where money has been withheld or misapplied by a fiduciary.¹¹⁶ Compound interest is awarded both on the amount of money which is owed by the defendant to the claimant and on the amount of interest which is already due to the claimant. Consequently, the award of compound interest is more favourable to the claimant.

In *Westdeutsche Landesbank Girozentrale v Islington London Borough Council*¹¹⁷ the issue for the House of Lords was whether compound interest was available in respect of all restitutionary claims. By a majority it was decided that, since the jurisdiction to award compound interest was equitable, compound interest could only be awarded in respect of equitable restitutionary claims. Consequently, where the claim was for money had and received the claimant could only obtain simple interest because this was a common law claim.¹¹⁸ The majority supported their conclusion by reference to a number of different arguments. In particular, they asserted that, since Parliament had decided in 1981 that simple interest should be awarded on claims at common law, it was not for the House of Lords to award compound interest in respect of such claims.¹¹⁹ But the Supreme Court Act 1981 does not specifically exclude the award of compound interest in respect of common law claims. Rather, it recognizes that the court can award simple interest for such claims. The equitable jurisdiction to award compound interest is still available in appropriate cases.

In two very strong dissenting judgments, Lords Goff and Woolf rejected the arguments of the majority. They asserted that, since the policy of the law of restitution was to remove benefits from the defendant, compound interest should be available in respect of all restitutionary claims, regardless of whether they arise at law or in equity.¹²⁰ This argument can be illustrated by the following example. In the straightforward case where the claimant pays money to the defendant by mistake and the defendant is liable to repay that money, the liability arises from

¹¹⁶ *President of India v La Pintada Compania Navigacion SA* [1985] AC 104, 116 (Lord Brandon).

¹¹⁷ [1996] AC 669.

¹¹⁸ In *Black v Davies* [2004] EWHC 1464, QB, it was recognized that compound interest could not be awarded in respect of damages awarded for the common law tort of deceit.

¹¹⁹ [1996] AC 669, 717 (Lord Browne-Wilkinson), 718 (Lord Slynn).

¹²⁰ *Ibid* 696 (Lord Goff), 736 (Lord Woolf).

the moment the money is received by the defendant, who has the use of it and so should pay the claimant for the value of that benefit. This was accepted by all the judges in the case. The difficulty relates to the valuation of this benefit. If the defendant was to borrow an equivalent amount of money from a financial institution, he or she would be liable to pay compound interest to that institution. It follows that the defendant has saved that amount of money and so this is the value of the benefit which the defendant should restore to the claimant, in addition to the value of the money which the defendant received in the first place.¹²¹ If it could be shown that, had the defendant borrowed the equivalent amount of money, the institution would only have paid simple interest, it would be appropriate for the interest awarded to the claimant to be simple rather than compound.¹²² Usually, however, the interest awarded in commercial transactions will be compound interest.¹²³

The approach of the minority is much more attractive than that of the majority since the award of compound interest is consistent with the fundamental principles underlying all restitutionary claims, especially that, where the defendant has obtained a benefit from the claimant in circumstances where the claimant can bring a restitutionary claim, the defendant should be required to make full restitution of all benefits obtained, regardless of the nature of the cause of action. The essential question relating to the award of interest turns on the valuation of the benefit which the defendant has obtained. Where the defendant has been saved paying compound interest to a financial institution as a result of receiving a benefit from the claimant, it is entirely appropriate that this benefit should be valued by reference to what the defendant has saved, namely the compound interest.

But despite the attraction of the views of the minority, the decision of the majority represents the law. It follows that compound interest is only available where the claimant brings a restitutionary equitable claim. This is indefensible. It is clear that a majority of the House of Lords did not feel that it is for the judiciary to change the law on the award of interest, so we must look to Parliament for statutory reform. What is needed is a statute which extends the equitable jurisdiction to award compound interest to include claims brought at common law. This has now been recognized by the Law Commission which has recommended that there should be a presumption that compound interest is available for awards over £15,000 or where the claimant has requested such interest.¹²⁴

The significance of compound interest for restitutionary claims has been recognized by the Court of Appeal in *Sempre Metals Ltd v IRC*.¹²⁵ This case was one of a number of cases arising from a decision of the European Court of Justice¹²⁶ that

¹²¹ Ibid 719 (Lord Woolf). See also *Black v Davies* [2004] EWHC 1464, QB, para 41 (McCombe J).

¹²² [1996] AC 669, 728 (Lord Woolf).

¹²³ *Sempre Metals Ltd v IRC* [2005] EWCA Civ 389, [2005] 3 WLR 521, 539, para 44 (Chadwick LJ).

¹²⁴ *Pre-judgment Interest on Debts and Damages* (Law Com. No. 287, 2004).

¹²⁵ [2005] EWCA Civ 389, [2005] 3 WLR 521.

¹²⁶ Cases C-397/98 and C-410/98 *Metallgesellschaft Ltd v IRC* [2001] Ch 620.

the English court had to provide for a compensatory or restitutionary claim where taxpayers had been required to pay tax early in breach of European Community law. It was recognized in *Sempre Metals* that, because the tax was due but was paid early, the restitutionary claim was grounded on the award of interest which should be measured as compound interest, because it 'is more likely to reflect economic reality and to provide full, rather than partial, recompense for the loss of the use of the money'.¹²⁷ It does not follow from this decision that compound interest will always be awarded at common law, because here the compound interest was being used to value the principal sum due to the claimant rather than being awarded in addition to the principal sum and the requirement to provide full compensation for the loss of use of the money derived from European Community law. However, the recognition that compound interest was the appropriate measure of interest is highly significant, and strengthens the argument that this measure of interest should be generally available to value the use of money.

7. The Role of Rescission within the Law of Restitution

One of the difficult questions facing the modern law of restitution concerns how the remedy of rescission should be fitted within the structure of the subject.

(a) Rescission as a remedy

(i) *The nature of rescission*

Where a transaction, usually a contract,¹²⁸ is voidable for fraudulent misrepresentation, duress¹²⁹ or non-disclosure¹³⁰ the claimant can set it aside at common law. Where it is voidable for non-fraudulent misrepresentation¹³¹ or undue influence¹³² the transaction can be set aside in equity.¹³³ Both at law and in equity the mechanism for setting the transaction aside is rescission. Once the claimant has set aside the transaction it is treated as vitiated and it follows that the parties should be returned to the position which they occupied before the transaction was entered into. This involves restitution of benefits transferred pursuant to the transaction.

Rescission has been described as a remedy¹³⁴ and it can be considered to have restitutionary consequences since a function of rescission is that the claimant can recover 'the property with which he has parted under the contract and [must

¹²⁷ [2005] EWCA Civ 389, [2005] 3 WLR 521, para 43 (Chadwick LJ).

¹²⁸ But the transaction may also be a gift or a voluntary settlement.

¹²⁹ *Whelpdale's case* (1605) 5 Co Rep 119a. ¹³⁰ *Ionides v Pender* (1874) LR 9 QB 531.

¹³¹ *Lamare v Dixon* (1873) LR 6 HL 414.

¹³² *Dunbar Bank plc v Nadeem* [1998] 3 All ER 876. See Chapter 10.

¹³³ Following *Great Peace Shipping Ltd v Tsalviris Salvage (International) Ltd* [2002] EWCA Civ 1407, [2003] AC 679 the equitable jurisdiction to grant rescission for common mistake has been rejected.

¹³⁴ *Dunbar Bank plc v Nadeem* [1998] 3 All ER 876, 884 (Millett LJ).

return] the benefit which he received' to the defendant.¹³⁵ This restitutionary consequence is available once the claimant has satisfied the conditions for setting the transaction aside, as recognized by Millett LJ in *Portman BS v Hamlyn Taylor and Neck*:¹³⁶

The obligation to make restitution must flow from the ineffectiveness of the transaction under which the money was paid and not from a mistake or misrepresentation which induced it . . . If the payer exercises his right of rescission in time and before the recipient deals with the money in accordance with his instructions, the obligation to make restitution may follow.

Often rescission will have monetary consequences because money paid by a claimant pursuant to a voidable transaction can be recovered as a consequence of rescission. This restitutionary consequence follows automatically from the rescission of the transaction, but it is also a condition of rescission, since the transaction cannot be set aside if the parties cannot be restored to their original position.

Rescission does not, however, always have restitutionary consequences. For example, sometimes the court may order rescission on terms, such as requiring the parties to enter into a new, more appropriate contract.¹³⁷ Where an executory contract is rescinded it has been suggested that the consequences of rescission are restitutionary, since the consequence of rescission in such circumstances is that the defendant is required to restore those rights against the claimant which derived from the contract.¹³⁸ These personal rights are benefits which were obtained under the contract and, if the contract is to be rescinded, they ought to be restored to the claimant. The better view, however, is that this does not involve restitution because there is no re-vesting of the benefit of contractual rights, rather those rights simply cease to exist at the moment of rescission.¹³⁹ The consequences of rescission will be restitutionary only if there is some benefit to be restored to the claimant.¹⁴⁰

(b) The process of rescission

The method by which the claimant rescinds a transaction depends on whether rescission occurs at law or in equity.¹⁴¹

¹³⁵ *Smith New Court Securities Ltd v Scrimgeour Vickers (Asset Management) Ltd* [1994] 2 BCLC 212, 221 (Nourse LJ).

¹³⁶ [1998] 4 All ER 202, 208.

¹³⁷ See p 35, below.

¹³⁸ Nahan, 'Rescission: A Case For Rejecting the Classical Model?' (1997) 27 Univ. WALR 66, 72.

¹³⁹ O'Sullivan, 'Rescission as a Self-help Remedy: A Critical Analysis' (2000) 59 CLJ 509.

¹⁴⁰ See *National Commercial Bank (Jamaica) Ltd v Hew* [2002] UKPC 65, para 43. In *Criterion Properties plc v Stratford UK Properties LLC* [2004] UKHL 28, [2004] 1 WLR 1846, 1855 Lord Scott recognized that the creation of contractual rights through an executory contract does not constitute the receipt of an asset and therefore it cannot constitute an enrichment.

¹⁴¹ See O'Sullivan (2000) 59 CLJ 509.

(i) Rescission at law

Where the claimant wishes to rescind a transaction at law he or she can do so without obtaining a court order.¹⁴² Consequently, rescission at law is a self-help mechanism. Where the claimant wishes to rescind a transaction it is usually necessary that he or she communicates this wish to rescind to the defendant. But in certain exceptional circumstances such direct communication is not required. For example, in *Car and Universal Finance Co Ltd v Caldwell*¹⁴³ the claimant wanted to rescind a contract to sell a car, but he could not trace the purchaser of the vehicle. It was held to be sufficient to rescind the contract that he had notified both the AA and the police that he wished them to assist him in finding the car. Alternatively, if there is a dispute about the right to rescind and the claimant commences judicial proceedings to resolve the matter, the statement in the particulars of claim that the transaction has been or should be set aside will in itself be sufficient to rescind the transaction.¹⁴⁴

(ii) Rescission in equity

Rescission in equity only occurs by order of the court. Or, perhaps more accurately, the claimant purports to rescind the transaction and the function of the court is to determine whether the claimant is entitled to do so and, if so, whether rescission has actually occurred.¹⁴⁵ Once the order of the court has been obtained, rescission will operate retrospectively to the date when the claimant commenced proceedings.¹⁴⁶

(c) Restitution following rescission

The restitutionary consequences which follow rescission can be analysed with reference either to the principle of vindicating property rights or the unjust enrichment principle, depending on whether the consequence of rescission is proprietary or personal.

(i) Proprietary

The proprietary consequences of rescission will be that, if the transaction is rescinded at law, legal title to property will be re-vested in the claimant.¹⁴⁷ Where the claimant rescinds the transaction in equity, the consequence will be that the property which the claimant transferred to the defendant will be held on trust for the claimant who will have an equitable proprietary interest in it.¹⁴⁸ In either case

¹⁴² *Car and Universal Finance Co Ltd v Caldwell* [1965] 1 QB 525, 532 (Lord Denning MR); *Brotherton v Aseguradora Cobeguros (No 2)* [2003] EWCA Civ 705, [2003] 3 All ER (Comm) 298, para 27 (Mance LJ).

¹⁴⁴ *TSB Bank plc v Camfield* [1995] 1 WLR 430, 438 (Roch LJ).

¹⁴⁵ *Ibid.* ¹⁴⁶ *Reese Silver Mining Co v Smith* (1869) LR 4 HL 64.

¹⁴⁷ *Car and Universal Finance Co Ltd v Caldwell* [1965] 1 QB 525. Cp. Swadling, 'Rescission, Property and the Common Law' (2005) 121 LQR 123 who argues that rescission at common law should not have proprietary consequences. See p 593, below.

¹⁴⁸ *El Ajou v Dollar Land Holdings plc* [1993] 3 All ER 717, 734 (Millet LJ).

the claimant will be able to bring a proprietary restitutionary claim to vindicate his or her property right.

(ii) *Personal*

Where the claimant has transferred property to the defendant under a voidable transaction which is rescinded, the defendant may not have retained the property or its traceable substitute, so that a proprietary restitutionary claim will not be available. The claimant will, however, be able to recover the value of the benefits transferred. This restitutionary response can be justified on the basis that, if the defendant was not required to make restitution to the claimant, the consequence of the claimant setting the transaction aside would be that the defendant is unjustly enriched at the claimant's expense.¹⁴⁹ This is because the defendant will have obtained a benefit from the claimant in circumstances where the defendant's retention of that benefit is unjust since the claimant had not intended the defendant to receive the benefit in those circumstances. Consequently, the real significance of the unjust enrichment principle for the purposes of rescission is that it has a negative function to ensure that the consequence of rescission is that the defendant will not be unjustly enriched.¹⁵⁰

Regardless of whether the transaction is rescinded at law or in equity, once it has been rescinded restitution follows automatically. The policy of the law is to return the parties to the position which they occupied before entering into the transaction. Consequently, the defendant will be obliged to return to the claimant all benefits which he or she received under the transaction and the claimant must make counter-restitution to the defendant.¹⁵¹ This restitution is typically in monetary form.¹⁵²

(d) **Bars to rescission**

The claimant's right to rescind a voidable transaction may be barred in certain circumstances.

(i) *Restitution and counter-restitution are impossible*¹⁵³

If the claimant and the defendant are not able to restore benefits received under a voidable transaction the orthodox view has been that rescission will be

¹⁴⁹ *National Commercial Bank (Jamaica) Ltd v Hew* [2002] UKPC 65, para 43.

¹⁵⁰ That the unjust enrichment principle can function in this negative way was recognized by the House of Lords in *Banque Financière de la Cité v Parc (Battersea) Ltd* [1999] 1 AC 221 where the remedy of subrogation was awarded to prevent the defendant from becoming unjustly enriched.

¹⁵¹ See *TSB Bank plc v Camfield* [1995] 1 WLR 430, 434–435 (Nourse LJ).

¹⁵² This is sometimes described as pecuniary rescission: Birks, 'Unjust Factors and Wrongs: Pecuniary Rescission for Undue Influence' [1997] RLR 72. This is misleading. Rescission involves setting aside the transaction; the pecuniary element relates to restitution following rescission.

¹⁵³ This principle is also known as the bar of *restitutio in integrum* being impossible. It is criticized by Nahan, (1997) 27 Univ. WALR 66, 76–79.

barred.¹⁵⁴ Traditionally, this principle has been interpreted as barring the right to rescind whenever restitution or counter-restitution cannot be made exactly. So, for example, it has been held that, where the claimant has consumed or disposed of property which was received from the defendant under a voidable contract, the claimant will be barred from rescinding the contract because counter-restitution cannot be made.¹⁵⁵ In *Smith New Court Securities Ltd v Scrimgeour Vickers (Asset Management) Ltd*¹⁵⁶ the claimant had been induced to buy shares as a result of the defendant's fraudulent misrepresentation. The Court of Appeal held that the claimant was unable to rescind the contract and recover the full purchase price of the shares from the defendant, because it had sold the shares to a third party and so was unable to make 'substantial restitution in specie of the property' which it had received.¹⁵⁷

This requirement to make precise restitution has proved to be a greater obstacle to rescission at law¹⁵⁸ than in equity, because equity has been more willing to value the benefits received so that, if it is no longer possible to restore property itself or the benefit is a service, the reasonable value of that property or service can be paid. Rescission should only be denied where it is not possible to value the benefit which has been provided. This is illustrated by *Newbigging v Adam*¹⁵⁹ where a contract had been rescinded for misrepresentation. The Court of Appeal held that the defendant was required to make restitution in respect of all benefits which he had received under the transaction. Consequently, the defendant was required to repay to the claimant the money which the claimant had put into a partnership business, as well as the money he had paid to discharge the debts of the business, minus those sums which the claimant had received from the partnership. An example concerning counter-restitution is *Erlanger v New Sombrero Phosphate Co*¹⁶⁰ where the claimant wished to rescind a contract for the purchase of a phosphate mine on the ground of non-disclosure of a material fact by the defendant. The problem was that the claimant had worked the mine and obtained some benefit from it. The House of Lords held that the claimant was able to rescind the contract, as long as it returned the mine to the defendant and accounted for the profits it had made from working the mine. As Lord Blackburn said, a court of equity will grant relief 'when-ever, by the use of its powers, it can do what is practically just, though it cannot restore the parties precisely to the state they were in before the contract'.¹⁶¹

¹⁵⁴ *Spence v Crawford* [1939] 3 All ER 271, 288–289 (Lord Wright); *Smith New Court Securities Ltd v Scrimgeour Vickers (Asset Management) Ltd* [1994] 2 BCLC 212, 221 (Nourse LJ) and *Dunbar plc v Nadeem* [1998] 3 All ER 876, 884 (Millett LJ).

¹⁵⁵ *Clarke v Dickson* (1858) EB and E 148; 120 ER 463. ¹⁵⁶ [1994] 2 BCLC 212.

¹⁵⁷ *Ibid* at p 221 (Nourse LJ). This issue was not raised on appeal before the House of Lords [1997] AC 254.

¹⁵⁸ See *Smith New Court Securities Ltd v Scrimgeour Vickers (Asset Management) Ltd* [1994] 2 BCLC 212, 221 (Nourse LJ).

¹⁵⁹ (1886) 34 Ch D 582. See also *O'Sullivan v Management Agency and Music Ltd* [1985] AC 686, *Cheese v Thomas* [1994] 1 WLR 129 and *Maboney v Purnell* [1996] 3 All ER 61.

¹⁶⁰ (1878) 3 App Cas 1218.

¹⁶¹ *Ibid* 1278. In the exercise of this power the court will also be prepared to grant the defendant an allowance in respect of the deterioration in value of any property which is returned to him or her.

The consequence of such decisions is that rescission will hardly ever be defeated in equity by the bar of restitution or counter-restitution not being possible, since restitution can be made in respect of virtually all benefits received if the benefit can be valued, even if it is not possible to return the specific benefit to the defendant.¹⁶² It is, however, most unfortunate that a similar approach to pecuniary restitution was not recognized for rescission at common law by the Court of Appeal in *Smith New Court Securities Ltd v Scrimgeour Vickers (Asset Management) Ltd*.¹⁶³ Surely it would have been sufficient for the claimant to pay the value of the shares to the defendant or to buy substitute shares which could be returned to the defendant. This was, in fact, recognized by Lord Browne-Wilkinson when the case was heard on appeal, although the question of rescission was not specifically considered by that court. Lord Browne-Wilkinson said that:

if the current law in fact provides (as the Court of Appeal thought) that there is no right to rescind the contract for the sale of quoted shares once the specific shares purchased have been sold, the law will need to be closely looked at hereafter. Since in such a case other, identical, shares can be purchased on the market, the defrauded purchaser can offer substantial *restitutio in integrum* which is normally sufficient.¹⁶⁴

This is surely the more just approach. It should follow that the bar of not being able to make restitution should only be relevant where the value of the benefit cannot be restored. Consequently, rescission will be barred and restitution denied only where the benefit obtained cannot be valued.¹⁶⁵

(ii) *Bona fide purchase for value*

Rescission in equity will be barred where a third party acquires an interest in assets other than money which were transferred under a voidable transaction, as long as the interest is acquired for some consideration and without notice of the defect which provides the reason for the claimant wishing to rescind it. This bar to rescission¹⁶⁶ operates in equity where the claimant with a right to rescind has what is called a mere equity. This equity will be defeated if somebody acquires a later legal¹⁶⁷ or equitable interest¹⁶⁸ in the property which the claimant had transferred under the transaction and that other person acquired the property for value and without notice of the claimant's equity to rescind.

The existence of this bar is, however, difficult to defend. Whilst it is clear that, if a third party has acquired proprietary rights in good faith and for value, the

¹⁶² See *Dunbar Bank plc v Nadeem* [1998] 3 All ER 876, 888 where Morritt LJ contemplated that, on the exceptional facts of that case, counter-restitution would not be possible.

¹⁶³ [1994] 2 BCLC 212. ¹⁶⁴ [1997] AC 254, 262.

¹⁶⁵ See Halson, 'Rescission for Misrepresentation' [1997] RLR 89, 91.

¹⁶⁶ Cp. the *defence* of *bona fide* purchase for value which operates to defeat restitutionary claims which are founded on the vindication of property rights. See Chapter 22.

¹⁶⁷ *Phillips v Brooks Ltd* [1919] 2 KB 243

¹⁶⁸ *Phillips v Phillips* (1862) 4 De GF and J 208; 45 ER 1164.

claimant should not be able to bring a proprietary claim against that property, it should not follow that the acquisition of third party proprietary rights should prevent the claimant from rescinding the transaction with the defendant and from recovering the value of the benefit which had been transferred to the defendant.¹⁶⁹

(iii) Affirmation

The claimant cannot rescind a transaction which he or she has affirmed. Two conditions must be satisfied before the transaction can be considered to have been affirmed.

(1) The claimant must know of the circumstances which enable him or her to rescind the transaction, as will be the case where the claimant discovers that he or she was induced to enter into the contract by virtue of the defendant's misrepresentation.¹⁷⁰ But rescission will not be barred if the claimant merely had the means of discovering that there was a ground for rescinding the transaction, even if this could have been discovered with due diligence.¹⁷¹

(2) The claimant must show by words or conduct that he or she has decided not to rescind the contract.¹⁷² It is not necessary for the claimant to communicate this affirmation to the defendant.¹⁷³ So, for example, in *Sharpley v Louth and East Coast Ry Co*¹⁷⁴ the claimant was induced by a misrepresentation of the defendant company to purchase shares in that company. The claimant sought to rescind the contract but was unable to do so because, having discovered that the defendant's representations had been untrue, he continued to act as a shareholder, for example by attending general meetings of the company. This was conduct which was considered to show that he intended to affirm the contract.

(iv) Lapse of time

The claimant will also be barred from rescinding a transaction if a reasonable period of time has elapsed before he or she has attempted to rescind it.¹⁷⁵ What constitutes a reasonable period of time is a question of fact which depends on the particular circumstances of the case. This bar is often difficult to distinguish from the bar of affirmation since, if the claimant delays unnecessarily before he or she seeks to rescind the transaction, this may be treated as affirmation of it.¹⁷⁶

¹⁶⁹ Nahan, (1997) 27 Univ. WALR 66, 74.

¹⁷⁰ *Car and Universal Finance Co Ltd v Caldwell* [1965] 1 QB 525.

¹⁷¹ *Redgrave v Hurd* (1881) 20 Ch D 1.

¹⁷² *Clough v London and North Western Ry Co* (1871) LR 7 Exch. 26.

¹⁷³ *Car and Universal Finance Co Ltd v Caldwell* [1965] 1 QB 525.

¹⁷⁴ (1876) 2 Ch D 663. ¹⁷⁵ *Leaf v International Galleries* [1950] 2 KB 86.

¹⁷⁶ *Clough v London and North Western Ry Co* (1871) LR 7 Exch. 26.

(e) Partial rescission and rescission on terms

It is a fundamental principle of the law of rescission that a transaction can only be rescinded in its entirety and not partially and that it is not possible to rescind a transaction on terms, such as by setting aside the whole transaction and substituting a new one for it.¹⁷⁷ This is illustrated by *TSB Bank plc v Camfield*¹⁷⁸ where it was held that a mortgage would be set aside completely as a result of a husband's misrepresentation and it would not be treated as valid to the extent of the maximum liability which the wife had accepted.

The apparent reason for the courts' refusal to allow partial rescission or rescission on terms stems from the perceived nature of rescission itself. Rescission is not considered to be a form of relief to which terms can be attached, but is a form of self-help. The claimant rescinds the transaction and the only role for the courts is to determine whether he or she has rescinded the transaction or is entitled to do so.¹⁷⁹ There is consequently no scope for any half-way house; either the claimant is or is not entitled to rescind the transaction in question. But, as has been seen, the better view is that rescission in equity does indeed depend on the intervention of the court. The court may be required to value a benefit received to secure restitution or counter-restitution. So why should it not be possible to impose other terms?¹⁸⁰

In fact, rescission on terms has been recognized, such as where a claimant wishes to rescind a transaction for mistake¹⁸¹ or undue influence.¹⁸² There will also be circumstances where it is appropriate to exercise judicial discretion to impose terms as a condition of rescission outside of the need to secure restitution as such. This discretion to impose terms could be justified on the basis that rescission should not be used to secure a result which can be characterized as unconscionable.¹⁸³ So if the claimant entered into a transaction as a result of misrepresentation thinking that he or she had entered into a surety transaction for £5,000 but in fact the transaction was for £50,000, the actual surety transaction should be rescinded, but terms be imposed that a £5,000 surety transaction should be substituted since this is the amount which the claimant actually consented to guarantee.

(f) The future of rescission

Rescission in equity is much more flexible than rescission at law. Increasingly the limitations of rescission at law are more difficult to defend. This is a situation where the equitable approach should take over,¹⁸⁴ so that all rescission should be

¹⁷⁷ *Zamet v Hyman* [1961] 1 WLR 1442. ¹⁷⁸ [1995] 1 WLR 430. See p 262, below.

¹⁷⁹ See Roch LJ, *ibid* 438. ¹⁸⁰ O'Sullivan (2000) 59 CLJ 509.

¹⁸¹ See *Solle v Butcher* [1950] 1 KB 671 and *Grist v Bailey* [1967] Ch 532.

¹⁸² *Cheese v Thomas* [1994] 1 WLR 129. See p 263, below.

¹⁸³ *Vadasz v Pioneer Concrete (SA) Pty Ltd* (1995) 69 ALJR 678, 684.

¹⁸⁴ O'Sullivan (2000) 59 CLJ 509, 528.

effected by means of a judicial order to which terms can be attached if necessary, rather than be treated simply as a self-help remedy. This was recognized by the Court of Appeal in *Great Peace Shipping Ltd v Tsavliris Salvage Ltd*¹⁸⁵ where it was recognized that

An equitable jurisdiction to grant rescission on terms where a common fundamental mistake has induced a contract gives greater flexibility than a doctrine of common law which holds the contract void in such circumstances. Just as the Law Reform (Frustrated Contracts) Act 1943 was needed to temper the effect of the common law doctrine of frustration, so there is scope for legislation to give greater flexibility to our law of mistake than the common law allows.

It is unfortunate that the Court felt that this creativity had to be a matter for Parliament rather than being developed by the courts.

¹⁸⁵ [2002] EWCA Civ 1407, [2003] QB 679, para 161.