Restitution Damages

An expectation damages measure gives the plaintiff the benefit of its bargain, putting them in the position they would have been if the contract had been performed. A reliance measure allows the plaintiff to recover expenditures made in reliance on the contract, restoring them to the pre-contract status quo ante. A restitution remedy instead allows the plaintiff to recover value conveyed on the defendant. The defendant must disgorge the benefit by which they have been unjustly enriched and return it to the other party. The restitution remedy is often described as an alternative to a contract remedy. The following cases explain when and to what extent that is true.

United States v. Algernon Blair, Inc.

479 F.2d 638 (4th Cir. 1973)

CRAVEN, Circuit Judge:

May a subcontractor, who justifiably ceases work under a contract because of the prime contractor's breach, recover in quantum meruit the value of labor and equipment already furnished pursuant to the contract irrespective of whether he would have been entitled to recover in a suit on the contract? We think so, and, for reasons to be stated, the decision of the district court will be reversed.

The subcontractor, Coastal Steel Erectors, Inc., brought this action under the provisions of the Miller Act, 40 U.S.C.A. § 270a et seq., in the name of the United States against Algernon Blair, Inc., and its surety, United States Fidelity and Guaranty Company. Blair had entered a contract with the United States for the construction of a naval hospital in Charleston County, South Carolina. Blair had then contracted with Coastal to perform certain steel erection and supply certain equipment in conjunction with Blair's contract with the United States. Coastal commenced performance of its obligations, supplying its own cranes for handling and placing steel. Blair refused to pay for crane rental, maintaining that it was not obligated to do so under the subcontract. Because of Blair's failure to make payments for crane rental, and after completion of approximately 28 percent of the subcontract, Coastal terminated its performance. Blair then proceeded to complete the job with a new subcontractor. Coastal brought this action to recover for labor and equipment furnished.

The district court found that the subcontract required Blair to pay for crane use and that Blair's refusal to do so was such a material breach as to justify Coastal's terminating performance. This finding is not questioned on appeal. The court then found that under the contract the

amount due Coastal, less what had already been paid, totaled approximately $37,000. Additionally, the court found Coastal would have lost more than $37,000 if it had completed performance. Holding that any amount due Coastal must be reduced by any loss it would have incurred by complete performance of the contract, the court denied recovery to Coastal. While the district court correctly stated the "'normal' rule of contract damages,"[1] we think Coastal is entitled to recover in quantum meruit.[2]

In *United States for Use of Susi Contracting Co. v. Zara Contracting Co.*, 146 F.2d 606 (2d Cir. 1944), a Miller Act action, the court was faced with a situation similar to that involved here–the prime contractor had unjustifiably breached a subcontract after partial performance by the subcontractor. The court stated:

> For it is an accepted principle of contract law, often applied in the case of construction contracts, that the promisee upon breach has the option to forego any suit on the contract and claim only the reasonable value of his performance.

146 F.2d at 610.... Quantum meruit recovery is not limited to an action against the prime contractor but may also be brought against the Miller Act surety, as in this case.[4] Further, that the complaint is not clear in regard to the theory of a plaintiff's recovery does not preclude recovery under quantum meruit. *Narragansett Improvement Co. v. United States*, 290 F.2d 577 (1st Cir. 1961). A plaintiff may join a claim for quantum meruit with a claim for damages from breach of contract.

In the present case, Coastal has, at its own expense, provided Blair with labor and the use of equipment. Blair, who breached the subcontract, has retained these benefits without having fully paid for them. On these facts, Coastal is entitled to restitution in quantum meruit.

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[1] Fuller & Perdue, *The Reliance Interest in Contract Damages*, 46 YALE L.J. 52 (1936); the first Restatement of Contracts § 333 (1932).

[2] Where there is a distinction between federal and state substantive law, federal law controls in actions under the Miller Act. *United States for Use and Benefit of Astro Cleaning & Packaging Co. v. Jamison Co.*, 425 F.2d 1281, 1282 n. 1 (6th Cir. 1970). But in this case the result would be the same, we think, under either state or federal law. *Compare United States for Use of Susi Contracting Co. v. Zara Contracting Co.*, 146 F.2d 606 (2d Cir. 1944), *with Gantt v. Morgan*, 199 S.C. 138, 18 S.E.2d 672 (1942).

[4] *Central Steel Erection Co. v. Will*, 304 F.2d 548, 552 (9th Cir. 1962); *Zara Contracting*, 146 F.2d at 612. This is consistent with the liberal construction which is given to the Miller Act to effectuate its protective purposes. See *United States ex rel. Sherman v. Carter*, 353 U.S. 210, 216-217, 77 S.Ct. 793, 1 L.Ed.2d 776 (1957).

The "restitution interest," involving a combination of unjust impoverishment with unjust gain, presents the strongest case for relief. 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. Fuller & Perdue, *The Reliance Interest in Contract Damages*, 46 YALE L.J. 52, 56 (1936).[6]

The impact of quantum meruit is to allow a promisee to recover the value of services he gave to the defendant irrespective of whether he would have lost money on the contract and been unable to recover in a suit on the contract. *Scaduto v. Orlando*, 381 F.2d 587, 595 (2d Cir. 1967). The measure of recovery for quantum meruit is the reasonable value of the performance, the first Restatement of Contracts § 347 (1932); and recovery is undiminished by any loss which would have been incurred by complete performance. 12 Williston on Contracts § 1485, at 312 (3d ed. 1970). While the contract price may be evidence of reasonable value of the services, it does not measure the value of the performance or limit recovery.[7] Rather, the standard for measuring the reasonable value of the services rendered is the amount for which such services could have been purchased from one in the plaintiff's position at the time and place the services were rendered.

Since the district court has not yet accurately determined the reasonable value of the labor and equipment use furnished by Coastal to Blair, the case must be remanded for those findings. When the amount has been determined, judgment will be entered in favor of Coastal, less payments already made under the contract. Accordingly, for the reasons stated above, the decision of the district court is

Reversed and remanded with instructions.

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[6] This case also comes within the requirements of the Restatements for recovery in quantum meruit. Restatement of Restitution § 107 (1937); the first Restatement of Contracts §§ 347-357 (1932).

[7] … It should be noted, however, that in suits for restitution there are many cases permitting the plaintiff to recover the value of benefits conferred on the defendant, even though this value exceeds that of the return performance promised by the defendant. In these cases it is no doubt felt that the defendant's breach should work a forfeiture of his right to retain the benefits of an advantageous bargain. Fuller & Perdue, supra at 77.

Notes and Questions

1. *Quantum meruit* is a Latin phrase that can be translated as "As much as he has deserved." The term can be further defined as "the reasonable value of services" or as "damages awarded in an amount considered reasonable to compensate a person who has rendered services in a quasi-contractual relationship." *Quantum Meruit*, Black's Law Dictionary (11th ed. 2019).

2. Many restitution cases grant recovery for value conveyed even though the contract or promise that the promisor allegedly breached turns out not to be enforceable. A contract may be unenforceable for any number of reasons – for example, the deal falls within the statute of frauds but was not memorialized in writing; the parties did not make a bargained for exchange or the promisee did not rely to her detriment on the promisor's promise; or the contract terms are too indefinite to enforce. But if a promisee has conveyed value on the promisor, she can often recover the value conveyed, even if the contract is otherwise unenforceable.

3. The Restatements (Second) of Contracts § 373, and (Third) of Restitution § 38(2)(b), *cmt* d & *ill.* 10, both support the rule in *Algernon Blair*: A contracting party that would recover nothing in expectation damages because they spent more in performing than the benefit of the bargain might recover the value conveyed on the breaching party. Thus, unlike reliance damages, which are typically capped by the expectancy, restitution damages are not.

4. As the court noted in *Algernon Blair*, *citing* Fuller & Perdue, this result might be justified because the laboring party has not only expended its effort, but the receiving party has been enriched by the labor. Failing to provide the laboring party a remedy would thus result in two injustices rather than one.

5. Reliance damages are typically greater than restitution damages. But unlike reliance damages, restitution damages are not necessarily capped by the benefit of the bargain, i.e., the claimant's expected profits. Consider the following hypothetical. Mezzrow contracts with Armstrong to provide the latter with musical arrangements in exchange for Armstrong's promise to publish the arrangements as sheet music and pay Mezzrow 15 percent of gross sales. Mezzrow invests 150 hours creating the arrangements, representing a cost to Mezzrow of $15,000 in foregone earnings, and delivers them to Armstrong. The value of the arrangements, measured by what Armstrong would have paid for the arrangements as a work made for hire, is $7,500. Armstrong wrongfully

breaches, and Mezzrow cannot prove that the benefit of the bargain can be estimated with reasonably certainty.

Mezzrow's reliance damages (his costs of performance writing the arrangements) are $15,000. His restitution damages are $7,500 (the value of the arrangements conveyed on Armstrong). If Armstrong can prove Mezzrow's royalties could not have exceeded $7,000, his reliance damages would be capped at $7,000. *See L. Albert & Son v. Armstrong Rubber Co.*. But under the holding in *Algernon Blair*, the restitution damages would not be so capped – Mezzrow would be entitled to recover the value conveyed on Armstrong, which it would be unjust for Armstrong to retain. *See* p. 3 & n.7, *supra*.

6. Consider the following hypothetical: Reinhardt contracts to sell his vintage guitar to Montgomery for $100,000. After Montgomery makes part payment to Reinhardt of $20,000, and purchases a custom display cabinet for $5,000, Reinhardt wrongfully refuses to transfer title. The market price of the guitar is only $70,000.

    a. What are Montgomery's expectation damages?

    b. What are Montgomery's reliance damages?

    c. What are Montgomery's restitution damages?

    d. Should a court withhold damages based on an argument from Reinhardt that his breach actually saved Montgomery $30,000 (the difference between the contract price and the value of the undelivered guitar) and thus Reinhardt should be allowed to retain the $20,000 part payment?

7. The Restatement (Third) of Restitution § 39 also offers a framework for when restitution is available as an alternative to expectancy. That section states that restitution is available as an alternative to expectancy *if* a deliberate breach of contract results in profits to the defaulting promisor *and* the available damages remedy is inadequate to protect the promisee. Does the subcontractor's case in *Algernon Blair* meet both of those elements?

8. Some courts have been willing to find value conveyed in cases where the promisor might reasonably argue they received no value. For example, in *Farash v. Sykes Datatronics, Inc.*, 59 N.Y.2d 500 (1983), a property owner and ostensible lessee agreed to a two-year lease that was not reduced to writing and was thus unenforceable. Pursuant to the deal, the owner modified the building to the lessee's specifications, but

the lessee refused to take possession. The Court of Appeals overturned dismissal of the owner's claims, holding that while the owner could not recover damages for the breach of the oral lease, they could recover "for the value of the work performed … in reliance on statements by and at the request of the [lessee]…. That defendant did not benefit from [the owner's] efforts does not require dismissal…" Two Justices dissented, arguing that the owner had not established unjust enrichment of the lessee necessary to support an award of quantum meruit.

9. Courts sometimes resist finding quantum meruit in cases where the party ostensibly conveying value is seen as an "officious intermeddler," one who conveys a benefit without having a valid reason for doing so. Thus, there is no restitution remedy for an unrequested benefit voluntarily conferred, unless the circumstances of the transaction justify the intervention of the claimant in the absence of an enforceable contract. *See* Restatement (First) of Restitution § 2 (1937).

* * *

Restitution is peculiar in another way. In some instances, a party will breach a contract, but the breaching party will also have conveyed value on the non-breaching party. The party in breach may not recover on the contract because it is they, and not the other party, who are in breach. But courts have considered whether the breaching party may nonetheless recover the value conveyed on the non-breaching party. The following case considers that question and adopts the now-disfavored common law rule on the issue.

Stark v. Parker

19 Mass. 267 (Supreme Judicial Court of Massachusetts 1824)

LINCOLN, J., delivered the opinion of the Court.

This case comes before us upon exceptions filed, pursuant to the statute, to the opinion, in matter of law, of a judge of the Court of Common Pleas, before whom the action was tried by a jury; and we are thus called upon to revise the judgment which was there rendered. The exceptions present a precise abstract question of law for consideration, namely, whether upon an entire contract for a term of service for a stipulated sum, and a part-performance, without any excuse for neglect of its completion, the party guilty of the neglect can maintain an action against the party contracted with, for an apportionment of the price, or a *quantum meruit,* for the services actually performed. Whatever may be the view properly taken of the contract between the parties in the case at bar, the point upon which it was ruled in the court below embraced but this single proposition. The direction to the jury was, "that although proved to

them, that the plaintiff agreed to serve the defendant for an agreed price for a year, and had voluntarily left his service before the expiration of that time, and without the fault of the defendant, and against his consent, still the plaintiff would be entitled to recover of the defendant, in this action, a sum in proportion to the time he had served, deducting therefrom such sum, (if any,) as the jury might think the defendant had suffered by having his service deserted." If this direction was wrong, the judgment must be reversed, and the case sent to a new trial, in which the diversity of construction given to the character and terms of the contract by the counsel for the respective parties may be a subject for distinct consideration.

It cannot but seem strange to those who are in any degree familiar with the fundamental principles of law, that doubts should ever have been entertained upon a question of this nature. Courts of justice are eminently characterized by their obligation and office to enforce the performance of contracts, and to withhold aid and countenance from those who seek, through their instrumentality, impunity or excuse for the violation of them. And it is no less repugnant to the well established rules of civil jurisprudence, than to the dictates of moral sense, that a party who deliberately and understandingly enters into an engagement and voluntarily breaks it, should be permitted to make that very engagement the foundation of a claim to compensation for services under it. The true ground of legal demand in all cases of contracts between parties is, that the party claiming has done all which on his part was to be performed *by the terms of the contract,* to entitle him to enforce the obligation of the other party.…

Upon examining the numerous authorities, which have been collected with great industry by the counsel for the plaintiff, it will be found, that a distinction has been uniformly recognised in the construction of contracts, between those in which the obligation of the parties is reciprocal and independent, and those where the duty of the one may be considered as a condition precedent to that of the other. In the latter cases, it is held, that the performance of the precedent obligation can alone entitle the party bound to it, to his action. Indeed the argument of the counsel in the present case has proceeded entirely upon this distinction, and upon the *petitio principii* in its application. It is assumed by him, that the service of the plaintiff for a year was not a condition precedent to his right to a proportion of the stipulated compensation for that entire term of service, but that upon a just interpretation of the contract, it is so far divisible, as that consistently with the terms of it, the plaintiff, having labored for any portion of the time, may receive compensation *pro tanto.* That this was the intention of the parties is said to be manifest from the fact found in the case, that the defendant from time to time did in fact make payments expressly toward this service. We have only to observe upon this point in the case, that how ever the parties may have intended between themselves, we are to look to the construction given to the contract by the court below. The jury were not

instructed to inquire into the meaning of the parties in making the contract. They were instructed, that if the contract was entire, in reference alike to the service and the compensation, still by law it was so divisible in the remedy, that the party might recover an equitable consideration for his labor, although the engagement to perform it had not been fulfilled. The contract itself was not discharged; it was considered as still subsisting, because the loss sustained by the defendant in the breach of it was to be estimated in the assessment of damages to the plaintiff. A proposition apparently more objectionable in terms can hardly be stated, and if supported at all it must rest upon the most explicit authority. The plaintiff sues in *indebitatus assumpsit* as though there was no special contract, and yet admits the existence of the contract to affect the amount he shall recover. The defendant objects to the recovery of the plaintiff the express contract which has been broken, and is himself charged with damages for the breach of an implied one which he never entered into. The rule that *expressum facit cessare tacitum,*[*] is as applicable to this, as to every other case. If the contract is entire and executory, it is to be declared upon. Where it is executed and a mere duty to pay the stipulated compensation remains, a general count for the money is sufficient. Numerous instances are indeed to be found in the books, of actions being maintained where the specific contract has not been executed by the party suing for compensation, but in every case it will be seen that the precise terms of the contract have been first held, either to have been expressly or impliedly waived, or the non-execution excused upon some known and settled principle of law.… Nothing can be more unreasonable than that a man, who deliberately and wantonly violates an engagement, should be permitted to seek in a court of justice an indemnity from the consequences of his voluntary act; and we are satisfied that the law will not allow it.

That such a contract as is supposed in the exceptions before us, expresses a condition to be performed by the plaintiff precedent to his right of action against the defendant, we cannot doubt. The plaintiff was to labor one year for an agreed price. The money was to be paid in compensation for the service, and not as a consideration for an engagement to serve. Otherwise, as no precise time was fixed for payment, it might as well be recovered before the commencement of the labor or during its progress, as at any subsequent period. While the contract was executory and in the course of execution and the plaintiff was in the employ of the defendant, it would never have been thought an action could be maintained for the precise sum of compensation agreed upon for the year. The agreement of the defendant was as entire on his part to pay, as that of the plaintiff to serve. The latter was to serve *one year,* the former to pay *one hundred and twenty dollars*. Upon the construction contended for by the plaintiff's

[*] A legal maxim that means "what is expressed makes what is implied silent." Eds.

counsel, that the defendant was to pay for any portion of the time in which the plaintiff should labor, in the same proportion to the whole sum which the time of labor done should bear to the time agreed for, there is no rule by which the defendant's liability can be determined. The plaintiff might as well claim his wages by the month as by the year, by the week as by the month, and by the day or hour as by either. The responsibility of the defendant would thus be affected in a manner totally inconsistent with the terms of his agreement to pay for a year's service in one certain and entire amount. Besides, a construction to this effect is utterly repugnant to the general understanding of the nature of such engagements. The usages of the country and common opinion upon subjects of this description are especially to be regarded, and we are bound judicially to take notice of that of which no one is in fact ignorant. It may be safe to affirm, that in no case has a contract in the terms of the one under consideration, been construed by practical men to give a right to demand the agreed compensation, before the performance of the labor, and that the employer and employed alike universally so understand it. The rule of law is in entire accordance with this sentiment, and it would be a flagrant violation of the first principles of justice to hold it otherwise.

The performance of a year's service was in this case a condition precedent to the obligation of payment. The plaintiff must perform the condition, before he is entitled to recover any thing under the contract, and he has no right to renounce his agreement and recover upon a *quantum meruit.* [*Citations omitted.*]

But it has been urged… a different rule of construction has been adopted in this commonwealth; and we are bound to believe that such has sometimes been the fact, from the opinion of the learned and respectable judge who tried this cause, and from instances of similar decisions cited at the bar, but not reported. The occasion of so great a departure from ancient and well established principles cannot well be understood. It has received no sanction at any time from the judgment of this Court within the period of our Reports. As early as the second volume of Massachusetts Reports, in the case of *Faxon v. Mansfield,* the common law doctrine in relation to dependent covenants was recognised and applied, and in several subsequent cases it has been repeated and uniformly adhered to. The law indeed is most reasonable in itself. It denies only to a party an advantage from his own wrong. It requires him to act justly by a faithful performance of his own engagements, before he exacts the fulfilment of dependent obligations on the part of others. It will not admit of the monstrous absurdity, that a man may voluntarily and without cause violate his agreement, and make the very breach of that agreement the foundation of an action which he could not maintain under it. Any apprehension that this rule may be abused to the purposes of oppression, by holding out an inducement to the employer, by unkind treatment near the close of a term of service, to drive

the laborer from his engagement, to the sacrifice of his wages, is wholly groundless. It is only in cases where the desertion is voluntary and without cause on the part of the laborer, or fault or consent on the part of the employer, that the principle applies. Wherever there is a reasonable excuse, the law allows a recovery. To say that this is not sufficient protection, that an excuse may in fact exist in countless secret and indescribable circumstances, which from their very nature are not susceptible of proof, or which, if proved, the law does not recognise as adequate, is to require no less than that the law should *presume* what can never legally be established, or should admit that as *competent,* which by positive rules is held to be wholly *immaterial*. We think well established principles are not thus to be shaken, and that in this commonwealth more especially, where the important business of husbandry leads to multiplied engagements of precisely this description, it should least of all be questioned, that the laborer is worthy of his hire, only upon the performance of his contract, and as the reward of fidelity.

The judgment of the Court of Common Pleas is reversed, and a new trial granted at the bar of this Court.

Notes and Questions

1. In *Stark*, the employer and employee agreed to a contract where the employee would work for a year, and the employer would pay for the work at the end of the year. Why might an employer want to bind the employee for the year? How do you suppose the employee took care of expenses for food and housing during that year?

2. If the employee can leave before the term has ended, and still be paid for the proportion of work done, has the non-breaching employer received the benefit of their bargain?

3. The court in *Stark* expresses skepticism that an employer would try to avoid paying by mistreating an employee nearing the end of the employment term. But there are circumstances where a contracting party utilizes violence or threats of violence to induce a counterparty to abandon their rights under the contract. For example, in the southern United States post-emancipation, some white landlords committed acts of violence against Black sharecroppers and tenants before the crops had matured. *See, e.g.*, Brittany Farr, *Breach by Violence*: *The Forgotten History of Sharecropper Litigation in the Post-Slavery South*, 69 UCLA L. REV. 674 (2022). In at least one case, an appellate court in Georgia held that the sharecropper was entitled to sue "on a quantum meruit, and recover the value of his labor in plowing, fencing, cultivating, and improving [the] land and premises." *Roberson v. Allen*, 7 Ga. App. 142, 142 (1909).

4. Ten years after *Stark*, a neighboring court held that a breaching employee could nonetheless recover the value of work conveyed. *Britton v. Turner*, 6 N.H. 481 (1834). The court in *Britton* differed from the court in *Stark* with regard to how likely an employer might be to mistreat an employee:

5. This rule, by binding the employer to pay the value of the service he actually receives, and the laborer to answer in damages where he does not complete the entire contract, will leave no temptation to the former to drive the laborer from his service, near the close of his term, by ill treatment, in order to escape from payment; nor to the latter to desert his service before the stipulated time, without a sufficient reason; and it will in most instances settle the whole controversy in one action, and prevent a multiplicity of suits and cross actions.

   Id. at 494-95. As mentioned in the next case, *Lancellotti v. Thomas*, the rule in *Britton* provides the more widely-followed modern trend in cases where the party in breach seeks restitution.

Lancellotti v. Thomas

341 Pa. Super. 1 (Superior Court of Pennsylvania 1985)

SPAETH, President Judge.

–1–

On July 25, 1973, the parties entered into an agreement in which appellant agreed to purchase appellees' luncheonette business and to rent from appellees the premises on which the business was located. Appellant agreed to buy the name of the business, the goodwill, and equipment; the inventory and real estate were not included in the agreement for the sale of the business. Appellees agreed to sell the business for the following consideration: $25,000 payable on signing of the agreement; appellant's promise that only he would own and operate the business; and appellant's promise to build an addition to the existing building, which would measure 16 feet by 16 feet, cost at least $15,000, and be 75 percent complete by May 1, [1974].

It was also agreed that appellees would lease appellant the property on which the business was operated for a period of five years, with appellant having the option of an additional five-year term. The rent was $8,000 per year for a term from September 1, 1973, to August 31, 1978. A separate lease providing for this rental was executed by the parties on the same date that the agreement was executed. This lease specified that the agreement to build the existing building was a condition of the lease. In exchange for appellant's promise to build the addition, there

was to be no rental charge for the property until August 31, 1973. Further, if the addition was not constructed as agreed, the lease would terminate automatically. An addendum, executed by the parties on August 14, 1973, modified this agreement, providing that "if the addition to the building as described in the Agreement is not constructed in accordance with the Agreement, the Buyer shall owe the Sellers $6,665 as rental for the property ..." for the period from July 25, 1973, to the end of that summer season. The addendum also provided that all the equipment would revert to appellees upon the appellant's default in regard to the addition.

Appellant paid appellees the $25,000 as agreed, and began to operate the business. However, at the end of the 1973 season, problems arose regarding the construction of the addition. Appellant claims that the building permit necessary to construct the addition was denied. Appellees claim that they obtained the building permit and presented it to appellant, who refused to begin construction. Additionally appellees claim that appellant agreed to reimburse them if they built the addition. At a cost of approximately $11,000, appellees did build a 20 feet by 40 feet addition. In the spring of 1974 appellees discovered that appellant was no longer interested in operating the business. There is no evidence in the record that appellant paid any rent from September 1, 1973, as the first rental payment was not due until May 15, 1974. Appellees resumed possession of the business and, upon opening the business for the 1974 summer season, found some of their equipment missing.

Appellant's complaint in assumpsit demanded that appellees return the $25,000 plus interest. Appellees denied that appellant was entitled to recovery of this sum and counterclaimed for damages totalling $52,000: $6,665 as rental for the property for the 1973 summer season and the remainder as compensation for "grievous damage to [appellees'] business, its goodwill and its physical operation ..." and appellee Lillian Thomas suffering "nervous illness, pain and suffering inclusive of serious bodily injury and necessitating bed rest and physicians' supervision for one year after [appellant's] default." Defendants' Counterclaim and New Matter, paras. 9–11. In his answer, Appellant only conceded liability for the $6,665 rent under the terms of the addendum…. The trial court, sitting without a jury, found against appellant on the original claim, allowing appellees to retain the $25,000 paid by appellant, and for appellees on the counterclaim, allowing them to recover the $6,665 rent.

–2–

At one time the common law rule prohibiting a defaulting party on a contract from recovering was the majority rule. J. Calamari and J. Perillo, The Law of Contracts § 11–26, at 427 (2d ed. 1977). However, a line of cases, apparently beginning with *Britton v. Turner,* 6 N.H. 481 (1834), departed from the common law rule. The merit of the common law rule was its recognition

that the party who breaches should not be allowed "to have advantage from his own wrong." Corbin, *The Right of a Defaulting Vendee to the Restitution of Installments Paid*, 40 YALE L.J. 1013, 1014 (1931). As Professor Perillo states, allowing recovery "invites contract-breaking and rewards morally unworthy conduct." *Restitution in the Second Restatement of Contracts,* 81 COLUM. L. REV. 37, 50 (1981). Its weakness, however, was its failure to recognize that the nonbreaching party should not obtain a windfall from the breach. The party who breaches after almost completely performing should not be more severely penalized than the party who breaches by not acting at all or after only beginning to act. Under the common law rule the injured party retains more benefit the more completely the breaching party has performed prior to the default. Thus it has been said that "to allow the injured party to retain the benefit of the part performance..., without making restitution of any part of such value, is the enforcement of a penalty or forfeiture against the contract-breaker." Corbin, *supra,* at 1013.

Critics of the common law rule have been arguing for its demise for over fifty years. *See* Corbin, *supra. See also* Calamari and Perillo, *supra,* at § 11–26; 5A Corbin on Contracts §§ 1122–1135 (1964); 12 S. Williston, A Treatise on the Law of Contracts §§ 1473–78 (3d ed. 1970). In response to this criticism an alternative rule has been adopted in the Restatement of Contracts.

The first Restatement of Contracts (1932) adopted the following rule:

> **§ 357. Restitution in Favor of a Plaintiff Who is Himself in Default.**
>
> (1) Where the defendant fails or refuses to perform his contract and is justified therein by the plaintiff's own breach of duty or non-performance of a condition, but the plaintiff has rendered a part performance under the contract that is a net benefit to the defendant, the plaintiff can get judgment, except as stated in Subsection (2), for the amount of such benefit in excess of the harm that he has caused to the defendant by his own breach, in no case exceeding a ratable proportion of the agreed compensation, if
>
> > (a) the plaintiff's breach or non-performance is not wilful and deliberate; or
> >
> > (b) the defendant, with knowledge that the plaintiff's breach of duty or non-performance of condition has occurred or will thereafter occur, assents to the rendition of the part performance, or accepts the benefit of it, or retains property received although its return in specie is still not unreasonably difficult or injurious.

> (2) The plaintiff has no right to compensation for his part performance if it is merely a payment of earnest money, or if the contract provides that it may be retained and it is not so greatly in excess of the defendant's harm that the provision is rejected as imposing a penalty.
>
> (3) The measure of the defendant's benefit from the plaintiff's part performance is the amount by which he has been enriched as a result of such performance unless the facts are those stated in Subsection (1b), in which case it is the price fixed by the contract for such part performance, or, if no price is so fixed, a ratable proportion of the total contract price.

In 1979, this rule was liberalized….[T]he first Restatement's exclusion of the willful defaulting purchaser from recovery was deleted, apparently in part due to the influence of the Uniform Commercial Code's permitting recovery by a buyer who willfully defaults.[1] *Id.,* Reporter's Note at 218. Professor Perillo suggests that the injured party has adequate protection without the common law rule.[2] Choosing "the just path," he therefore rejects the common law rule, explaining this choice by saying that times have changed. "What appears to be just to one generation may be viewed differently by another." Perillo, *supra,* at 50….

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[1] In Pennsylvania, 13 Pa.C.S. § 2718, provides:

> § 2718. Liquidation or limitation of damages; deposits
>
> (a) Liquidated damages in agreement.—Damages for breach by either party may be liquidated in the agreement but only at an amount which is reasonable in the light of the anticipated or actual harm caused by the breach, the difficulties of proof of loss, and the inconvenience or nonfeasibility of otherwise obtaining an adequate remedy. A term fixing unreasonably large liquidated damages is void as a penalty.
>
> (b) Right of buyer to restitution.—Where the seller justifiably withholds delivery of goods because of the breach of the buyer, the buyer is entitled to restitution of any amount by which the sum of his payments exceeds:
>
> (1) the amount to which the seller is entitled by virtue of terms liquidating the damages of the seller in accordance with subsection (a); or
>
> (2) in the absence of such terms, 20% of the value of the total performance for which the buyer is obligated under the contract or $500, whichever is smaller.

[2] He identifies four types of protection:

> First, the defaulting party's right to recovery is subject to the aggrieved party's right to offset his damages. Second, the measure of benefit is limited to the actual enrichment and cannot exceed a ratable portion of the contract price. Third, restitution is denied to the extent that the criteria for a valid liquidated damages clause are present. Fourth, restitution is denied if the aggrieved party seeks and is entitled to specific performance.

Perillo, *supra,* at 50 (footnotes omitted).

Many jurisdictions have rejected the common law rule and permit recovery by the defaulting party [citing cases].

This development has been called the modern trend [citing authorities].

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In Pennsylvania, the common law rule has been applied to contracts for the sale of real property. *Kaufman Hotel & Restaurant Co. v. Thomas,* 411 Pa. 87 (1963); *Luria v. Robbins,* 223 Pa.Super. 456 (1973). In such cases, however, the seller has several remedies against a breaching buyer, including, in appropriate cases, an action for specific performance or for the purchase price. *See Trachtenburg v. Sibarco Stations, Inc.,* 477 Pa. 517 (1978). *See also* 5A Corbin on Contracts, *supra,* § 1145.

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The common law rule has also been applied in Pennsylvania to contracts for the sale of goods. *Atlantic City Tire and Rubber Corp. v. Southwark Foundry & Machine Co.,* 289 Pa. 569 (1927). However, Pennsylvania has since adopted the Uniform Commercial Code, which, as to contracts for the sale of goods, has modified the common law rule by 13 Pa.C.S. § 2718(b), which permits a breaching party to recover restitution. *See* note 2, *supra.*

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In regard to the present case, § 374 of the Restatement (Second) of Contracts represents a more enlightened approach than the common law rule. "Rules of contract law are not rules of punishment; the contract breaker is not an outlaw." Perillo, *supra,* at 50. The party who committed a breach should be entitled to recover "any benefit ... in excess of the loss that he has caused by his own breach." Restatement (Second) of Contracts § 374(1).

This conclusion leads to the further conclusion that we should remand this case to the trial court. The trial court rested its decision on the common law rule…. Thus it never considered whether appellant is entitled to restitution, Restatement (Second) of Contracts § 374(1), nor, if appellant is not entitled to restitution, whether retention of the $25,000 was "reasonable in

the light of the anticipated or actual loss caused by the breach and the difficulties of proof of loss," *id.,* § 374(2).[5]

Remanded for further proceedings consistent with this opinion. Jurisdiction relinquished.

TAMILIA, Judge, dissenting:

I strongly dissent. In the first instance, the majority does not and cannot cite *any* Pennsylvania authority adopting the rule cited in § 374 of the Second Restatement of Contracts. Although the ostensible basis for remand is the trial court's reliance on outmoded law, the majority relies on law so new as to be virtually unknown in this jurisdiction. The law in Pennsylvania has been and continues to be that where a binding contract exists, and there is no allegation that the contract itself is void or voidable, a breaching party is not entitled to recovery. *Luria v. Robbins,* 223 Pa.Super. 456 (1978). While our Supreme Court may yet abrogate the forfeiture principle in this Commonwealth, it has not yet seen fit to do so, and we may not usurp its prerogatives, particularly when the result would be unjust.

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Notes and Questions

1. The Restatements of Contract and the Restatement (Third) of Restitution have embraced what the *Lancellotti* court calls the modern trend. The Restatement (Third) of Restitution states in § 36(1) that "A performing party whose material breach prevents a recovery on the contract has a claim in restitution against the recipient of performance, as necessary to prevent unjust enrichment." That benefit conveyed will be reduced by the costs incurred due to the laboring party's own breach.

2. Consider the following: Moran contracts to build McBride's house for $200,000. Moran abandons the job after part performance. A court finds Moran in material breach, so she cannot secure damages for breach.

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[5] … We are remanding so that the trial court may consider whether appellant is entitled to restitution. If the trial court again finds that it was the intention of the parties that the $25,000 be retained in the event of a breach… then the court must determine whether this sum is reasonable. If the sum is unreasonable, appellant is entitled to restitution. *See* Restatement (Second) of Contracts § 374, Comment c.

But Moran provided a value of $150,000 in labor and materials furnished. McBride paid Moran $100,000 in progress payments prior to the breach. Thus, Moran conveyed $50,000 of value on McBride for which she has not been paid.

After Moran abandoned the job, McBride paid Spaulding $150,000 to finish the job. On completion, the house is worth $210,000, but it cost McBride $250,000 to have it finished. Thus, McBride's expectation damages are $40,000. Therefore, Moran's recovery in restitution would be reduced by McBride's frustrated expectancy, and Moran can recover only $10,000. *Compare* Rest. 3d Rest. § 36, *ill. 2, 4*.

3. Note 3 of the opinion in *Lancelloti* explains that section 2-718 of the UCC allows restitution to the breaching buyer. For more on the operation of that provision, consider *Neri v. Retail Marine*.

4. The UCC provides that a non-breaching buyer may also seek restitution. Upon seller's breach, and in addition to the other remedies listed in UCC § 2-711, the buyer may "recover[] so much of the price as has been paid…" But the seller receives an expectation damages remedy for goods that the buyer has accepted, rather than a restitution measure. UCC § 2-607(1) (the seller can recover at the contract rate for any goods the buyer has accepted).