ARTICLE

COMPENSATION FORFEITURE: STACKING REMEDIES AGAINST DISLOYAL AGENTS AND EMPLOYEES

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I. INTRODUCTION

"[T]his is equity, not rocket science."[1]

The median CEO compensation package for the top 100 highest paid CEOs was worth $23.8 million in 2014.[2] That is much more than we pay the President of the United States[3] or justices of the Supreme Court[4] but is similar to the median for the 100 highest paid athletes in the world, $23.95 million (including endorsement income).[5] Those who believe

1. *In re* Alpha Telcom, Inc., No. CV 01-1283-PA, 2005 WL 488675, at *29 (D. Or. Aug. 18, 2004).

2. Press Release, Equilar, Equilar and the New York Times Release Top 200 Highest-Paid CEO Ranking 2015 (May 18, 2015), http://www.equilar.com/press-releases/31-equilar-and-the-new-york-times-release-top-200-highest-paid-CEO-Ranking-2015.html.

3. *See Salaries*, HOUSE PRESS GALLERY, http://pressgallery.house.gov/member-data/salaries (last visited Dec. 11, 2015) (reporting the yearly salary of the President as $400,000).

4. *See id.* (stating the salary of the Chief Justice and the Associate Justices as $258,100 and $246,800, respectively).

5. According to *Forbes*'s *The World's 100 Highest-Paid Athletes*, in 2015 the median pay, including endorsement income, was $23.95 million, and the average was $32 million. By category of sport, the average pay after endorsement income and the number of athletes in each category are as follows: boxing ($160.8 million for three); tennis ($34.8 million for seven); golf ($34.8 million for six); soccer ($32.3 million for fifteen); cricket ($31 million for one); racing ($30.1 million for six); basketball ($29.3 million for eighteen); football ($25.6 million for sixteen); baseball ($23.3 million for twenty-seven); and track ($21.0 million for one). *The World's Highest-Paid Athletes*, FORBES, http://www.forbes.com/athletes/list/#tab:overall (last visited Dec. 11, 2015).

executives are overpaid may find some solace in the fact that when a senior business executive is sued for breach of fiduciary duty, one of the biggest penalties he faces will be in proportion to his elevated compensation. From that point of view, the effect of forfeiting three to five years of gross compensation is similar to that of an Aikido expert who turns the momentum of his opponent against him; i.e., forfeiture turns the defendant's high compensation into a large potential liability for disloyalty.

Compensation forfeiture is a simple but substantial enhancement for the remedies awarded for a breach of fiduciary duty. Thus, if the principal proves the fiduciary accrued a hidden profit, the principal can secure the disgorgement of the profit and, in addition, can plead for compensation forfeiture for the same disloyalty. It may constitute a principal's only remedy and it frequently exceeds compensatory and consequential damages. Pleading for forfeiture does not exclude any other damage claim or remedy and requires no special proof or expert testimony. The principal or employer can readily identify and prove the measure of the compensation, which includes the fiduciary's salary, commissions, fees, bonuses and retirement benefits. Grants of stock or stock options can also be forfeited in kind as specific restitution in equity.

The principles underlying compensation forfeiture against disloyal fiduciaries date back in the law of equity to before 1600. When a fiduciary's act of disloyalty is regarded as a breach of an implied condition that the fiduciary will be loyal, compensation forfeiture also has support in contract law.

The dual goals for remedying a breach of fiduciary duty lead to multiple remedies for a single cause of action, which include a mix of remedies in equity and at law that are stacked on top of one another. When the remedy package includes disgorgement, compensation forfeiture, and punitive damages, it consists of three remedies, which are each intended to deter future disloyalty, but that deterrence can only be justified in total if there is no limit or ceiling on the deterrent effect of remedies as they grow ever larger. Some critics assert compensation forfeiture poses a risk for possible abuse by employers who use the device to control employees' personal lives by threatening it against their First Amendment rights.

In most courts today, compensation forfeiture is awarded in a manner similar to punitive damages; it is stacked on top of other remedies when the defendant's disloyalty is found to warrant such an additional remedy. Alternatively, compensation forfeiture is implicit in disgorgement or an accounting, which generally deny the disloyal fiduciary's compensation as a legitimate expense when measuring unjust enrichment.

The term, "breach of fiduciary duty" or even "disloyalty" sometimes fails to adequately denote the egregious nature of the fiduciary's betrayal that is substantiated in the trial. Some courts have acknowledged the egregiousness of the defendant's behavior can have an impact on finding liability and the measure of the remedies awarded.[6] Especially in cases with egregious or prejudicial facts, forfeiture's role as quasi-punitive damages may, therefore, be heightened. At times, the sum of compensation forfeiture and punitive damages can exceed 500% of the plaintiff's compensatory and consequential damages. Even if it is not the specific intent, awarding remedy packages with such high ratios can be expected to financially ruin defendants.

Stacking punitive damages on top of disgorgement and compensation forfeiture is only possible in a court system that has been merged because such a combination of remedies is contrary to the traditional principles and safeguards of courts in equity and courts at law. The size of such packages can fluctuate greatly given the combination of egregious case facts, the absence of traditional safeguards, and the subjective nature of the trial judge's equitable discretion.

If disloyal executives were a rational group of fiduciaries who weighed risks and rewards, the threat of forfeiting three to five years of their gross compensation would deter all but the largest schemes of fraud and theft. Yet, for many of the executives described in this Article, the dollar amount of proven gains to the defendants was only a fraction of the amount of compensation they forfeited. The defendants' basic irrationality is further confirmed by the fact that they were highly compensated and did not need to steal. Moreover, their refusal to reconcile or confess at any point along way, led to each being fired, convicted, punished, and ruined.

Section II of this Article considers the cases of five innovative and successful (albeit felonious) CEOs and explores the consequences of becoming such a corporate outlaw. A review of the case opinions reveals compensation forfeiture amounted to a majority of the non-punitive damages in each case. Section III briefly evaluates how the characteristics of a claim for breach of fiduciary duty can result in a stacked package of remedies, promoting a combination of remedies of great variety but without the limits on the size or punishment components of the package.

6. *See* George P. Roach, *Texas Remedies in Equity for Breach of Fiduciary Duty: Disgorgement, Forfeiture, and Fracturing*, 45 ST. MARY'S L.J. 367, 427–28 (describing how egregious case facts relating to betrayal changed remedies law in two cases); *see also* 1 DAN B. DOBBS, LAW OF REMEDIES § 4.1(4), at 570 (2d. ed. 1993) ("If the wrong is bad enough, even a radical remedy that captures the defendant's own property to protect the plaintiff's rights may be acceptable." (citations omitted)).

Thereafter, Section IV discusses the key elements and issues in advocating or defending a claim of compensation forfeiture. Section V will briefly discuss some alternative approaches, such as asset forfeiture and innocent misrepresentation, which are sometimes employed in fiduciary claims.

An article is shaped, for better or worse, by the choices employed to limit its scope. In this Article, while cases relating to fiduciary claims against lawyers are included, the current controversy about dual claims for legal malpractice and breach of fiduciary duty is not addressed in the detail it deserves. Similarly, alternative remedies in equity are discussed only in comparison with or in combination with forfeiture.

Given the Article's national scope, generalizations supported by examples from a variety of the jurisdictions that support or modify the main view can only highlight some of the key issues without fully considering each state's position on each issue. Opinions from New York, Illinois, Texas, California, and Massachusetts will receive disproportionate attention because their courts are the most active practitioners of forfeiture.

The Article will manifest certain semantic preferences that should be noted. In the belief that the term "equitable" is a semantic chameleon that can be easily misunderstood, it is used as infrequently as possible.[7] This Article will use the term "remedy in equity" rather than "equitable remedy." Since it is believed that "unjust enrichment" denotes a cause of action—both at law and in equity—as well as a remedy in equity,[8] this Article will employ "disgorgement" to denote the remedy in equity.

7. *See* Alt. Unlimited, Inc. v. New Balt. City Bd. of Sch. Comm'rs, 843 A.2d 252, 277 (Md. Ct. Spec. App. 2004) ("Contrasted with that . . . sweeping and essentially clichéd meaning of 'equitable' is 'equitable' as it more carefully distinguishes an 'equitable remedy' from a 'legal remedy,' each with its own attendant procedures and consequences."); RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 4 reporter's note c (AM. LAW INST. 2011) ("A statement to the effect that 'restitution is equitable' is a harmless platitude so long as 'equity' means only 'fairness.' The same statement becomes mischievous when it is offered as the basis for defining the jurisdiction of courts or agencies, or the kinds of relief they are authorized to administer.").

8. *See generally*, Douglas Laycock, *The Scope and Significance of Restitution*, 67 TEX. L. REV. 1277 (1989) ("'Restitution' means recovery based on and measured by unjust enrichment."); Douglas L. Johnson & Neville L. Johnson, *What Happened to Unjust Enrichment in California? The Deterioration of Equity in the California Courts*, 44 LOY. L.A. L. REV. 277 (2010) (asserting "[r]estitution has . . . evolved into its own recognized body of law, with unjust enrichment as its guiding principle"); Doug Rendleman, *When Is Enrichment Unjust? Restitution Visits an Onyx Bathroom*, 36 LOY. L.A. L. REV. 991 (2003) (stating "[o]rganizing restitution under the general principle of unjust enrichment found favor" in the 1937 Restatement (First) of Restitution and Unjust Enrichment); Paul T. Wangerin, *The Strategic Value of Restitutionary Remedies*, 75 NEB. L. REV. 255 (1996) (proclaiming "most practicing lawyers generally know that restitutionary remedies have something to do with 'unjust enrichment'").

II. CORPORATE OUTLAWS

Some of the more notorious outlaws of the old-West have been romanticized by folk songs, novels and movies. The corporate outlaws described in this Article seem unlikely candidates for such glorification. Our country has plenty of criminals who cheat and steal, but these convicted executives are unusual because they were so successful in their legitimate business endeavors that they did not need to steal the additional money to feed their families, to send their children to college, or to pay for a lifestyle well beyond the desires of most Americans today. Indeed, the discovery that these defendants suffered from a gambling addiction would at least tend to explain some of the criminal chaos that many of them seemed to seek out so compulsively.

As a point of reference, these felons might be compared with modern bank robbers. The average bank robbery in the United States in 2011 resulted in a gross loss of less than $10,000 per robbery.[9] The total cash and securities stolen in the 5,086 bank robberies in 2011[10] of $38.3 million represents less than half of the $102.5 million production budget for *Public Enemies*,[11] a 2009 movie about the ruthless Depression-era bank robber, John Dillinger. Alternatively, when Ian Gittlitz defrauded his company, ICD Publications, Inc., of $1,220,623 in unauthorized advances and fraudulent expense reimbursements,[12] he committed the equivalent of more than 160 bank robberies.[13]

9. *See Bank Crime Statistics for Federally Insured Financial Institutions, January 1, 2011–December 31, 2011*, THE FEDERAL BUREAU OF INVESTIGATION, https://www.fbi.gov/stats-services/publications/bank-crime-statistics-2011/bank-crime-statistics-2011 (last visited Dec. 11, 2015) (tallying all robberies, larcenies, and burglaries for a total of 5,086 violations in which $38,343,502 were stolen, resulting in a rate of $7,539 per robbery).

10. According to FBI data, the number of bank robberies (at federal insured institutions) decreased from 7,644 in 2003 to 5,086 in 2011. Similarly, the gross amount taken declined from $77.1 million to $38.3 million and the average amount taken declined from $10,086 to $7,538. For analysis of the data from 2003 and 2011, compare *Bank Crime Statistics for Federal Insured Financial Institutions, January 1, 2003–December 31, 2003*, U.S. DEP'T JUST., https://www.fbi.gov/stats-services/publications/bank-crime-statistics-2003/bank-crime-report-2003-pdf (last visited Dec. 11, 2015), with *Bank Crime Statistics for Federally Insured Financial Institutions, January 1, 2011–December 31, 2011*, *supra* note 9.

11. *See Public Enemies (2009)*, NUMBERS, http://www.the-numbers.com/movie/Public-Enemies (last visited Dec. 11, 2015) (reporting the budget for *Public Enemies* was $102.5 million).

12. *See* ICD Publ'ns, Inc. v. Gittlitz, 2014 IL App (1st) 133277, ¶ 34 (noting, from 2000 to 2007, "Gittlitz received[,] through 'unsupported checks' [and] . . . 'advances' written to himself, . . . $1,220,523").

13. Of course, this overlooks the eighty-eight injuries (principally to bank personnel) and thirteen deaths (principally to the perpetrators) in 2011. *Bank Crime Statistics for Federally Insured Financial Institutions, January 1, 2011–December 31, 2011*, *supra* note 9.

In contrast with armed bank robbers, these corporate outlaws worked their way into positions of power and influence through their legitimate success. They earned the respect and trust of their shareholders and directors. They did not appear suddenly at corporate headquarters, menacing their board of directors with guns and demanding access to the corporate vault. They were invited into the boardroom where they were delegated control over corporate personnel and large amounts of assets and money based on the respect and trust they had legitimately earned over a long period of success. But, as disloyal fiduciaries, they breached their duty and betrayed that trust on numerous occasions.

Because of the size of the claims and the corporate-employers, the four cases are not meant to be representative in size of a typical case; but instead, each serves to show how the combination of remedies can vary. The remedy packages differ, but some important similarities stand out despite the difference in company size and date:

- The defendants were all successful CEOs, some of whom transformed their industries;
- All but one defendant enjoyed annual compensation in excess of $1 million;
- All were found guilty of at least one felony (only one served significant jail time);
- None of them confessed and surrendered to the mercy of the employer or the court;
- Based on compensation damages awarded, the average amount of money stolen per time period amounted to less than 25% of the executive's compensation;
- Compensation forfeiture contributed to a majority of the non-exemplary damages for each one;[14] and
- Punitive damages were awarded against three of the defendants.

A. *Richard Grassgreen: You Don't Tug on the Robes of a Judge in Equity*

In 1969, Perry Mendel founded Kinder–Care, Inc. (KC), which rapidly grew to become the largest provider of child care in the United States by 1989.[15] As the national chain grew and prospered, the company diversified and began supporting financial and insurance services and

14. *See infra* App. 1.

15. Enstar Grp., Inc. v. Grassgreen, 812 F. Supp. 1562, 1564–65 (M.D. Ala. 1993).

related specialty retail product lines.[16] Richard Grassgreen helped establish the company as Mendel's second in command.[17] In the 1980s, Grassgreen operated as a director of the company and held titles ranging from executive vice president to chief operating officer.[18] In 1989, the company was effectively split into two separate companies: Kinder–Care Learning Centers, Inc. (KCLC), which owned and operated the day care operations, and The Enstar Group, Inc. (Enstar), which marketed the ancillary services and specialty retail products.[19] The reorganization gave Mendel control of KCLC by himself and gave Grassgreen control of Enstar, each as chairman of the board and CEO.[20]

The investment activities that formed the primary source of liability occurred solely in 1985 and 1986.[21] From 1987 to 1989, their disloyalties were found to be their failure to disclose or volunteer information about their prior investments.[22] In 1990, the disloyalties were expanded to also include misrepresentation and concealment of evidence.[23]

Until KC was reorganized in 1989, Grassgreen had exclusive authority over KC's investment operations.[24] In the mid-1980s, Mendel and Grassgreen formed the partnership, Megra Partners (Megra), which made investments for the personal gain of the two equal partners.[25]

In their early days, during the 1970s and early-1980s, their investment banker, Mike Milken of the firm, Drexel Burnham Lambert, Inc. (Drexel),[26] was instrumental in providing the company with access to outside investment capital to support the company's rapid growth.[27] As the company's operations grew and blossomed, KC no longer required outside capital as it generated substantial amounts of cash in excess of

16. *Id.* at 1565.

17. *See id.* (establishing Mendel as KC's President and Grassgreen as KC's executive vice president).

18. *See id.* ("Grassgreen was Kinder–Care's Executive Vice President and Director and . . . . then became President and Chief Operating Officer of Kinder–Care . . . .").

19. *Id.*

20. *Id.*

21. *See id.* at 1566–68 (recounting the disloyal investing activities of the defendants from 1985 to 1986).

22. *See id.* at 1572–73 (expressing Grassgreen continued to suppress and withhold information about his self-dealings from KC's board of directors from 1987 to 1989).

23. *Id.* at 1573.

24. *Id.* at 1565.

25. Enstar Grp., Inc. v. Grassgreen, 812 F. Supp. 1562, 1565 (M.D. Ala. 1993).

26. In the interest of full disclosure, the author was an investment banker for Drexel from 1975 to 1980 and 1989 to 1990 but never worked on the KC account.

27. *See id.* at 1565–68 (detailing some of the agreements and activities between Megra and Drexel that fostered Megra's growth at KC's expense).

what was needed to maintain and grow existing operations.[28] Mendel and Grassgreen sought out Milken's help for advice on how to invest the company's surplus cash.[29]

While KC was growing and prospering in the late '70s and early '80s, so were Drexel and Mike Milken.[30] By March 1985, Drexel was actively involved in financing large corporate mergers, friendly or not, with large amounts of junk bonds.[31] Indeed, Drexel's annual conference for investors in Beverly Hills during the takeover craze (the so-called Predators' Ball) was notorious throughout the 1980s.[32]

Given the conditional nature of making a merger (friendly) or takeover (unfriendly) offer, which required shareholder and regulatory approval, the financial facilities for such projects required substantial flexibility. Therefore, Drexel and other investment bankers provided the putative buyer with pools of short-term, standby capital (similar in theory to a line of credit).[33] During such a project, the would-be buyer would pay a commitment fee of 0.75% for a standby financing facility.[34] The fee represented payment for the investor's commitment to provide financing if and when the merger proposal succeeded.[35]

Mendel's and Grassgreen's primary breaches of duty related to their arrangement for Megra to receive the standby fees while KC made the commitment to invest when and if required.[36] This practice, which clearly shows at least disloyalty, could also be described as self-dealing or fraud, but the simplest term for it is embezzlement or theft of option fees.

28. *See id.* at 1566 ("Kinder–Care was generating large amounts of income which were being invested outside the business in an extensive investment portfolio.").

29. *See id.* ("As investment manager for Kinder–Care, Grassgreen invested substantial sums of the corporation's money through Drexel.").

30. *Id.* at 1565–66.

31. *Id.* at 1562, 1565 n.3 ("The bonds were called 'junk' because they were considered too risky to be investment quality bonds. While the risk associated with these bonds was significantly higher than other types of investments, the returns were also significantly higher.").

32. For one view of Drexel Burnham Lambert's role in the investment activity in mergers and takeovers at that time, see generally CONNIE BRUCK, THE PREDATORS' BALL: THE INSIDE STORY OF DREXEL BURNHAM AND THE RISE OF THE JUNK BOND RAIDERS (Penguin Books 1988).

33. *See Grassgreen*, 812 F. Supp. at 1565–66 ("Milken developed a procedure whereby money wasn't actually raised, initially[,] . . . . [making] sure that there were individuals or entities lined up who agreed to finance the takeover . . . . These agreements . . . were called commitments[,] [and] [i]n return for committing . . . Milken would pay a fee to those individuals or entities.").

34. *See id.* at 1566 ("These fees were normally 0.75% of the amount committed.").

35. For example, for KC's commitment to invest $10 million, Megra received a fee of $75,000. *See id.* (showing how Megra was able to exploit this commitment fee process to use KC's money to accrue commitment fees for itself).

36. *Id.* at 1565–66 ("Drexel paid . . . commitment fees for Kinder–Care's agreement to invest in transactions . . . . These fees, however, were instead paid to Megra . . . .").

Megra received fees for which it provided no consideration and for which KC was liable to provide funding.[37] In 1985 and 1986, Megra received $695,000 in standby fees[38] that required $49 million of investment by KC.[39] In addition, Megra arranged for KC and its affiliates to invest $51 million more in an arbitrage partnership known as Cohen Feit.[40] As a result of KC's investment, Megra was granted a limited partnership interest in the general partner and received payments of $430,731.[41]

In total, Megra earned $1,125,731 in commitment fees and partnership distributions, while KC invested approximately $100 million in takeover securities and a private arbitrage fund.[42] KC did receive dividend and interest payments on the takeover securities, but it also had to pay for the income taxes on Megra's commitment fees and other partnership income because Megra used KC's tax identification number.[43]

Megra also accrued gains from investment opportunities gained from KC's participation in the Drexel takeover investments. In 1985, Megra was offered the opportunity to purchase warrants in the acquisition vehicle that purchased Storer Communications as an additional return on KC's investment of roughly $5 million in the related acquisition financing.[44] The warrants were purchased with $15,224 from the Megra account through MacPherson Partners.[45] These warrants earned a total profit of $674,000, which was paid in January and March of 1989 (the MacPherson Investment).[46] In March 1986, Megra also invested $165,000 of the commitment fees to purchase the common stock of THL Industries, Inc.,

37. *See id.* at 1566 ("Kinder–Care money was invested or committed, but instead of Kinder–Care receiving the fees paid in exchange for the investment or commitment, the fees were kept by the individual officers and directors who had committed the investment of their corporation's money.").

38. *Id.* at 1569 n.10.

39. *Id.* at 1566–67.

40. *Id.* at 1567.

41. *Id.*

42. *Id.* at 1566–68. The amounts committed by KC were $16 million for ANR, $18 million for Pantry Pride, $10 million for Pacific Lumber, $51 million for Midcon, and $5 million for Storer Communications, totalling $100 million in commitments. *Id.* Megra, on the other hand, received $105,000 for ANR, $112,500 for Pantry Pride, $50,000 for Pacific Lumber, $225,000 for GAF, $202,500 for Midcon, $430,731 for the Cohen Feit override, totaling $1,125,731 in fees. *Id.* In addition, Megra made subsequent profits of $674,000 on Storer Communications stock and $586,461 on THL Industries, Inc. stock. *Id.*

43. *See* Enstar Grp., Inc. v. Grassgreen, 812 F. Supp. 1562, 1566 (M.D. Ala. 1993) ("While Megra received the commitment fee, Grassgreen used Kinder–Care's tax I.D. number to report the income.").

44. *Id.* at 1567.

45. *Id.* at 1567–68.

46. *Id.*

which was later sold for a profit of $586,461 (the THL Investment).[47]

Starting sometime in the mid-1980s, a number of accusations were directed at Wall Street, and especially at Drexel and Mike Milken, concerning securities fraud, insider trading, and negligent standards for underwriting junk bonds.[48] Market practices on junk bonds, standby investments, and takeover financing were also investigated by Rudy Giuliani, a U.S. attorney in the Southern District of New York, and by other government entities.[49]

Enstar's board of directors hired special outside counsel in January 1990 to investigate allegations that Mendel and Grassgreen had personally retained the warrants that KC should have received for its investment in MacPherson.[50] Throughout the investigation, Grassgreen denied receiving any commitment fees and failed to disclose any of Megra's activities.[51] At a cost of $260,395, that investigation found no wrongdoing, and Enstar reimbursed Grassgreen an additional $68,552 for his legal expenses during the investigation.[52] However, Mendel and Grassgreen disgorged the profit they received in the MacPherson Investment; although they retained their interest in the MacPherson entity.[53]

Mendel and Grassgreen continued to stonewall and failed to disclose any additional information until Giuliani's investigation revealed records of the standby fees.[54] Roughly eight to nine months after first learning of the possible scandal, Enstar's board of directors allowed Grassgreen to resign in October 1990.[55] On October 19, 1990, Grassgreen also pled guilty to one count of mail fraud relating to the receipt of commitment fees and one count of securities fraud relating to the MacPherson

47. *Id.* at 1568.

48. *See id.* (noting there was "a wide-ranging U.S. Attorney's investigation of Drexel and Milken").

49. *Id.* (reporting the findings of the U.S. Attorney's investigation).

50. *Id.*

51. *Id.*

52. *Id.*

53. *See* Enstar Grp., Inc. v. Grassgreen, 812 F. Supp. 1562, 1568 n.9 (M.D. Ala. 1993) (explaining how the "gratuity" theory of profit forfeiture justified Grassgreen and Mendel disgorging their profits).

54. *See id.* at 1568 (emphasizing records were missed by the special counsel's investigation and noting, "Grassgreen's misrepresentations, along with the disappearance from Megra's records of the Drexel documents, concealed the payment of commitment fees until records showing the fees were discovered in Drexel's papers by the U.S. Attorney in October[] 1990 during his investigation of Drexel").

55. *Id.*

Investment.[56] However, even after entering into the consent decree, Mendel and Grassgreen made no restitution to Enstar for any of the other commitment fees.[57]

Enstar's initial complaint was filed against both Mendel and Grassgreen.[58] Subsequently, Mendel settled with Enstar for an additional $4.5 million.[59] It is also worth noting, by the time of the actual trial, Enstar had filed for bankruptcy, meaning the lawsuit was pursued by either the debtor in possession or a bankruptcy trustee.[60]

Acknowledging that hindsight is more profound than foresight, it is interesting to consider Grassgreen's position at the end of 1990. Around that time, Grassgreen enjoyed a net worth of about $26.9 million[61] and probably could have settled his liability somewhere between $1.95 million, the eventual amount of compensatory damages,[62] and $4.5 million, the settlement for Mendel.[63] Thus, with minimal repercussions other than having to testifying against Drexel and Milken as required under his plea bargain, Grassgreen could have resolved his criminal and civil liability with plenty of net worth to spare. Whatever calculation he did make, it seems unlikely that he took into account possible liability for $5.2 million of forfeited compensation for the prior five years (or punitive damages of $10 million more). Instead, he chose to stonewall Enstar's civil claims which resulted in a net civil award of $15 million in addition to the costs of defending the civil claim.[64]

Even though Grassgreen had already made some reimbursements and plead guilty to two felonies, he entered the civil trial unrepentant and in denial of his disloyalty.[65] The trial judge specifically referred to Grassgreen's attempt to hide or shield his assets[66] and disregarded

56. *Id.* at 1569.

57. *See id.* at 1569 n.10 (reconciling each component of the $1,947,550 of compensation damages without any adjustment for any payments by Grassgreen).

58. *Id.* at 1569.

59. *Id.*

60. *Id.* at 1574.

61. *Id.* at 1580.

62. *Id.* at 1569 n.10.

63. Enstar Grp., Inc. v. Grassgreen, 812 F. Supp. 1562, 1569 (M.D. Ala. 1993).

64. *Id.* at 1584 (including $1,947,550 for a compensatory award by the jury, $5,197,663 for compensation forfeiture, $586,462 for the THL profit, $548,461 for interest, and $10 million for punitive damages, totaling $18,280,464).

65. *See id.* at 1574 (explaining Grassgreen believed it would be unfair for the corporation to have received his services without compensation).

66. *Id.* at 1580.

testimony that neither he nor the jury found credible.[67] From his opinion, it is clear the judge was concerned with Grassgreen's egregious disloyalty and the need to restore investors' trust in corporate officers and directors.[68]

The trial was conducted in two parts. In the main case, the jury found Grassgreen liable for breach of fiduciary duty and awarded Enstar compensatory damages of $1,947,550[69] (which were largely uncontested) and punitive damages of $18 million.[70] Thereafter, the jury was dismissed, and the parties contested the issues of compensation forfeiture, adjustments to the compensatory damages, and the reasonableness of the jury's punitive damages award.[71]

This case is a strong example of the unique relief sometimes achieved with remedies in equity. Certainly compensation forfeiture is a uniquely advantageous remedy for the plaintiff as it is not mutually exclusive with any other remedy and need not relate to any damage or loss to the principal.[72] However, in this case, the other remedies in equity and the process of measuring remedies in equity also increased the size of the total package of remedies. For a claim of breach of fiduciary duty at law, damages are measured as of the date of the tort.[73] Thus, compensatory damages would be limited to the lost commitment fees and the costs of

67. *See, e.g.*, *id.* at 1566–67 nn.4–5 & 7 (referencing various statements made by Grassgreen that were disregarded or unconvincing to the jury).

68. *See id.* at 1582 ("The court has addressed earlier its strong feelings concerning the crucial importance to this country's economic system of corporate officers and directors understanding clearly that their first duty is to their corporations, and not to themselves.").

69. *Id.* at 1569 n.10.

70. *Id.* at 1569.

71. *See id.* at 1571 (noting the court determined the residual issues after the jury found there was breach of fiduciary duty).

72. *See id.* at 1574 (ignoring Grassgreen's argument—claiming he should not have to forfeit compensation because there was no harm to the company—stating, "Damage to the corporation is not required to be shown[] because it is not relevant to this issue"); *see also* RESTATEMENT (SECOND) OF AGENCY § 469 cmt. a (AM. LAW INST. 1958) ("An agent is entitled to no compensation for a service which constitutes a violation of his duties . . . . This is true even though the disobedience results in no substantial harm to the principal's interests.").

73. Arthur Andersen & Co. v. Perry Equip. Corp., 945 S.W.2d 812, 814–16 (Tex. 1997) (holding the measure of out-of-pocket damages for fraudulent inducement must be distinguished between direct damages (loss in value as of the date of the tort) and consequential damages (further loss in value after the date of the tort) and incidental or reliance damages). More recently, a rule allowing a company to "claw back any compensation earned after the start of the wrongdoing" against an officer for breaching a fiduciary duty has been applied to reach similar results. Aaron D. Jones, *Corporate Officer Wrongdoing and the Fiduciary Duties of Corporate Officers Under Delaware Law*, 44 AM. BUS. L.J. 475, 515 (2007).

investigation.[74]

Conversely, the measure of a remedy in equity is based on an accounting in equity, which is based on different evidentiary principles and presumptions developed over the last 500 years to process claims against trusts and fiduciaries.[75] The measure of a remedy in equity is based on ex post data as current as the date of trial.[76] Therefore, the measure of the damages should include any subsequent gains the defendant accrued with the principal's money and its proceeds.[77]

For remedies in equity based on accounting in equity, the ex post gains of some investments do not have to be offset by the losses of the other investments that declined in value between the date of the tort and the date of trial. Accounting in equity allows the claimant to pick which investments are to be valued at the date of the tort and which on the date of trial. The principal is entitled to treat each investment separately and accept or reject the actual results of each separate transaction.[78]

74. *See Grassgreen*, 812 F. Supp. at 1583 (noting compensatory damages included commitment fees and costs of the investigation).

75. *See* RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 51 cmt. a (AM. LAW INST. 2011) ("Restitution measured by the defendant's wrongful gain is frequently called 'disgorgement.' Other cases refer to an 'accounting' or an 'accounting for profits.' Whether or not these terms are employed, the remedial issues in all cases of conscious wrongdoing are the same."); *see also* Doug Rendleman, *Measurement of Restitution: Coordinating Restitution with Compensatory Damages and Punitive Damages*, 68 WASH. & LEE L. REV. 973, 994 (2011) ("Accounting, also known as disgorgement, is a vehicle for equitable restitution that is not based on a res or fund. It does not require the plaintiff to trace 'her' asset."). *See generally* Joel Eichengrun, *Remedying the Remedy of Accounting*, 60 IND. L.J. 463 (1985) (exploring the remedy of accounting).

76. *See* Rubber Co. v. Goodyear, 76 U.S. (9 Wall.) 788, 804 (1870) ("The rule is founded in reason and justice. It compensates one party and punishes the other. It makes the wrong-doer liable for actual, not possible, gains. The controlling consideration is that he shall not profit by his wrong."); Allen v. Devon Energy Holdings, LLC, 367 S.W.3d 355, 410 (Tex. App.—Houston [1st Dist.] 2012) ("The uncertainties . . . as to how many shares Allen would have kept absent the alleged fraudulent inducement and when he would have sold those shares do not pose an obstacle to a potential disgorgement remedy because there is no dispute over what Devon paid to acquire Chief."), *pet. granted*, *judgm't vacated w.r.m.*, No. 12-0253, 2013 Tex. LEXIS 20 (Tex. Jan. 11, 2013); *see also* Laycock, *supra* note 8, at 1284 (explaining restitutionary claims matter when liability arises through unjust enrichment or when the plaintiff has a particular preference or need of it).

77. *See generally* Roach, *supra* note 6 (discussing the use of equitable remedies for breaches of fiduciary duty).

78. George P. Roach, *Counter-restitution for Monetary Remedies in Equity*, 68 WASH. & LEE L. REV. 1271, 1277–78 (2011) (noting "[i]f the breaches of trust, however, are not separate and distinct, the trustee is accountable only for the net gain or chargeable only with the net loss resulting therefrom"). Further,

> [w]ithout the anti-netting rule, a trustee under certain circumstances might be inclined to commit multiple breaches of trust: "For example, the trustee whose misconduct has caused a loss may take improper risks in pursuit of extra profits if those profits may serve to eliminate or reduce the amount of expected surcharge."

Effectively, each investment is treated as a separate count and the principal is free to choose between remedies in equity or remedies at law for each one.[79]

Without any discussion of adequate remedy or irreparable injury,[80] the court effectively granted the remedy in equity of a constructive trust against Megra and its holdings of the commitment fees and other special investments that Megra purchased with the proceeds of the commitment fees.[81] The effect of a constructive trust is twofold: (1) it provides a lien for the principal's claim and (2) it requires a formal process of accounting that allows the principal to trace the proceeds of its lost assets and funds in order to recognize any subsequent enhancements in value.[82] Such an accounting also credits the principal for any interim dividends, splits, or exchanges that represent increases in value.

To similar effect, the court granted the remedy in equity, specific restitution, for Megra's interest in MacPherson Partners. Specific restitution transfers possession of an asset to the claimant, enabling the principal to capture any income earned or appreciation in the asset's value subsequent to when the defendant wrongly gained possession.[83] Similar

Id. (quoting Charles E. Rounds, Jr., *Relief for IP Rights Infringement Is Primarily Equitable: How American Legal Education Is Short-Changing the 21st Century Corporate Litigator*, 26 SANTA CLARA COMPUTER & HIGH TECH. L.J. 313, 350 (2010)).

79. *See* UNJUST ENRICHMENT § 51(5)(b) ("A conscious wrongdoer or a defaulting fiduciary who makes unauthorized investments of the claimant's assets is accountable for profits and liable for losses."); RESTATEMENT (SECOND) OF TRUSTS § 213 cmt. a (AM. LAW INST. 1959) (illustrating how portions of a trust are treated separately in cases of breach); *see also* George P. Roach, *Unjust Enrichment in Texas: Is It a Floor Wax or a Dessert Topping?*, 65 BAYLOR L. REV. 153, 162 (2013) (discussing the rationale and wide-spread application for the anti-netting rule).

80. *See* discussion *infra* Section IV.B.

81. *See* Enstar Grp., Inc. v. Grassgreen, 812 F. Supp. 1562, 1575 (M.D. Ala. 1993) (rejecting Grassgreen's argument that profits should be offset by the Megra account's losses).

82. *See* United States v. Carter, 217 U.S. 286, 309 (1910) (discussing the doctrine of constructive trust). The Court explains:

> If an agent to sell effects a sale to himself, under the cover of the name of another person, he becomes, in respect to the property, a trustee for the principal; and, at the election of the latter, seasonably made, will be compelled to surrender it, or, if he has disposed of it to a bona fide purchaser, to account not only for its real value, but for any profit realized by him on such resale. And this will be done upon the demand of the principal, although it may not appear that the property, at the time the agent fraudulently acquired it, was worth more than he paid for it.

Id. (quoting Robertson v. Chapman, 152 U.S. 673, 681–82 (1894)); *see also* Rendleman, *supra* note 75, at 991 ("In addition to measuring recovery by the defendant's gains when the plaintiff may not be able to prove compensatory damages, a plaintiff may seek equitable restitution through a constructive trust to recover specific property and to outrank defendant's other creditors.").

83. *See* Laycock, *supra* note 8, at 1284 ("The restitutionary claim matters in three sets of cases: (1) when unjust enrichment is the only source of liability; (2) when plaintiff prefers to measure

to a constructive trust, specific restitution also generally "primes" any lien subsequently placed on the asset after the defendant gained possession.

The opinion provides a detailed analysis of Grassgreen's activities and management responsibilities coinciding with his disloyal acts establishing a pervasive pattern of disloyalty and causation.[84] Grassgreen's actions were also found to be highly egregious.[85] The possibility of apportioning Grassgreen's compensation, forfeiting less than 100% of the compensation actually paid, was discussed in Judge Albritton's opinion as a theoretical possibility.[86] Judge Albritton acknowledged that a judge in equity enjoys substantial discretion and that partial forfeiture was possible but inappropriate for Grassgreen's case, emphasizing his flagrant disloyalty.[87]

The opinion thoroughly analyzes the jury's award of punitive damages.[88] The judge reviewed a number of factors and issues, but his decision to reduce the punitive damages from $18 million to $10 million was not transparent.[89] He concluded $10 million in punitive damages would be a more reasonable award than $18 million.[90] One interesting factor he considered was that Grassgreen was not expected to serve much time in jail or prison.[91]

Under Alabama law, exemplary damages are intended to punish but not destroy the defendant,[92] so Judge Albritton reviewed Grassgreen's net

recovery by defendant's gain, either because it exceeds plaintiff's loss or because it is easier to measure; and (3) when plaintiff prefers specific restitution, either because defendant is insolvent, because the thing plaintiff lost has changed in value, or because plaintiff values the thing he lost for nonmarket reasons.").

84. *See Grassgreen*, 812 F. Supp. at 1571–73 (chronicling Grassgreen's trail of misrepresentation and dishonesty from 1985–90).

85. *See id.* at 1579 ("Grassgreen's conduct was truly reprehensible. He evinced an arrogant and callous disregard for his duties . . . . Rather than giving his corporation the benefit of commitment fees and lucrative investment opportunities, or of honestly telling his directors about these dealings and seeking their approval, he secretly took the money for himself.").

86. *See id.* at 1574 (recognizing "there is room for judicial discretion in this matter" but electing to "enforce . . . as forcefully as possible").

87. *See id.* (finding "Richard Grassgreen breached his duty flagrantly").

88. *Id.* at 1576–82 (discussing punitive damages in terms of the statutory cap and the potential excessiveness of the award).

89. *See id.* at 1582 (noting the jury's goal was to send a warning message to corporate officers and a "$10,000,000 punitive award in this case should certainly accomplish that purpose").

90. *See id.* (determining $10 million in punitive damages acted as a sufficient deterrent).

91. *See id.* at 1581 (attributing the lighter sentence to "the fact that the New York court was rewarding Grassgreen for helping to convict Milken, and also to the fact that the New York court did not have the benefit of all of the evidence which is before this court showing the egregiousness of Grassgreen's breach of trust").

92. *See id.* at 1580–81 (listing financial condition and appropriate deterrence as factors in

worth and ability to pay punitive damages. The judge took exception to Grassgreen's testimony that his net worth declined so precipitously from $26.9 million in June 1990 to $3.0 million at trial in 1993.[93] His review noted Grassgreen's inventory of assets at trial did not include an asset valued at $20 million in 1990:

> The Plaintiff presented evidence that tended to show that, through a series of transactions involving Grassgreen's wife and related companies, this stock has, in effect, been converted into an investment now held in the name of Grassgreen's wife[,] which will provide periodic payments to Mr. and Mrs. Grassgreen over the next 14 years in excess of $19,000,000. Without analyzing the effect of those transactions on creditors of Grassgreen, the court finds that, at the very least, this evidence shows efforts on Grassgreen's part to shield assets. The court does not consider Grassgreen's testimony concerning his financial position to be credible.[94]

As a result, Grassgreen possibly learned the first of two key reasons why you must not try to deceive a federal judge that sits in equity: you will be more likely to experience justice rather than mercy in his holdings. Thus, the exemplary damages were only reduced from $18 million to $10 million, which was likely to be necessary to survive review from the Eleventh Circuit.[95] The final judgment of $15,017,698 reflects a credit of $3,262,765 for Mendel's settlement payments of $4,798,183.[96]

No public record has been found indicating whether Enstar succeeded in fully collecting the judgment. However, it seems likely that in that process, Grassgreen may have learned the second key reason not to annoy the judge: his orders are issued under his in personam authority as a judge sitting in equity.[97] In similar circumstances some judges have sent a defendant to jail for failing to satisfy an order.[98]

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determining a just punitive damages award).

93. *See id.* at 1580 (noting "[t]he court does not consider Grassgreen's testimony concerning his financial position to be credible").

94. *Id.*

95. Compensatory damages amounted to only $1.95 million; therefore, if punitive damages amounted to $18 million, the ratio of punitive to compensatory damages would have been 9.2. *See id.* at 1569 (assessing compensatory damages at $1,947,550 and punitive damages at $18 million). For further discussion of ratios of punitive to actual damages, see *State Farm Mutual Automobile Insurance Co. v. Campbell*, 538 U.S. 408, 424–25 (2003).

96. *Grassgreen*, 812 F. Supp. at 1584.

97. *See* 1 DOBBS, *supra* note 6, § 2.2, at 73–74 ("The command was personal[,] and there were echoes in it of the [K]ing's political power of an earlier era. When he disobeyed, there was something like lese majesty, and he was clamped in irons as punishment for his disobedience.").

98. *See* Pierce v. Vision Invs., Inc., 779 F.2d 302, 309 (5th Cir. 1986) ("Because the court's order in the present case is an equitable decree designed to protect the public and to permit effective

Loyalty, ethics, and criminal issues aside, the takeover investments seemed to produce only a small return for the risks involved. KC had to invest $49 million and $51 million to generate just $625,000 in commitment fees and $431,000 in partner distributions to Megra. Given the acknowledged expertise and experience of Mendel and Grassgreen in the child-care industry, it is likely they could have found some better use for $100 million of investment capital than buying takeover junk bonds. An alternative investment in operations, for example, might have helped Enstar avoid bankruptcy in 1993.

B. *William Aramony: The Richard Nixon or Pete Rose of the Nonprofit Sector*[99]

Aramony v. United Way of America[100] is a case about the former CEO of United Way, William Aramony, a 59-year-old married man that pursued multiple affairs at the same time with women in his offices and stole money from the national charity that he made famous. Even though there was substantial evidence of his disloyalties (including his conviction for twenty counts of criminal fraud based on the testimony of his personal staff), his employer was only awarded compensatory damages for a small portion of the expenses of conducting an internal investigation.[101] Perhaps not surprising for a charity, the board of directors suffered difficulties and indecision in reacting to the Aramony scandal and in seeking reimbursement for what proved to be serious losses from declining contributions.

Under the leadership of William Aramony, United Way grew to become the nation's largest community funder. During his administration, United Way formed an alliance with the National Football League in 1975.[102] In

enforcement of the Interstate Land Sales Full Disclosure Act, a judgment of contempt designed to enforce that order is entirely appropriate."); C.C. Langdell, *A Brief Survey of Equity Jurisdiction*, 1 HARV. L. REV. 111, 117 (1887) ("[I]f a court of equity decides that the defendant in a suit ought to pay money or deliver property to the plaintiff, . . . it commands the defendant personally to pay the money or to deliver possession of the property, and punishes him by imprisonment if he refuse[s] or neglect[s] to do it.").

99. *See Old Battles and New Challenges*, NONPROFIT TIMES (Apr. 1, 2002), http://www.thenonprofittimes.com/news-articles/old-battles-and-new-challenges ("There are some names within areas of American culture that conjure up conflicting emotions. In politics, there's Richard Nixon. In baseball, it's Pete Rose. For the nonprofit sector, it's William Aramony.").

100. Aramony v. United Way of Am. (*Aramony II*), 28 F. Supp. 2d 147 (S.D.N.Y. 1998), *aff'd in part*, *rev'd in part sub nom.* Aramony v. United Way Replacement Benefit Plan (*Aramony III*), 191 F.3d 140 (2d Cir. 1999).

101. *Id.* at 176, 182, 185.

102. *See Old Battles and New Challenges*, *supra* note 99 ("Under his watch, the system extended its impact domestically and internationally—most visibly through its partnership with the National

1991, the last full year before the scandal broke, United Way consisted of approximately 2,100 local groups that raised almost $3.2 billion annually and voluntarily pledged about $24 million to the United Way "headquarters" or United Way of America (UWA), which provides technical support and services to the local groups.[103]

His salary for the last full year was $390,000.[104] He "supplemented" that income illicitly in two ways: forming independent companies (off balance sheet) that "served" the employer–company and extensively abusing UWA's expense and reimbursement system.[105]

He was a colorful public figure that attracted media attention. According to various news reports, Aramony's problems in 1991 actually began in 1986 when he met Lisa Villasor Thomas, age twenty-two, on an airplane. They became acquainted, and he offered her a job at his headquarters where they started their affair.[106] That relationship, ended when Aramony met Lisa's seventeen-year-old sister, Lori Villasor, who had recently graduated from high school.[107] Thus began the spectacle in New York of the fifty-nine-year-old CEO of United Way being sighted in public in the company of an attractive young lady who was not old enough to be his niece.[108] According to the seventy-one-count indictment, Aramony spent UWA's money to maintain Lori's lavish lifestyle in midtown Manhattan.[109] Aramony's explanation was disingenuity disguised as altruism; he stated at one point, "[Lori] comes from a poverty background. I don't want her to slip back into it."[110]

Football League.").

103. *Aramony II*, 28 F. Supp. 2d at 165–66.

104. *Id.* at 156.

105. *Id.* at 156–57 nn.4–5 (discussing Aramony's questionable "spin-off" companies and recounting some of the personal expenses he billed to UWA for reimbursement).

106. Laurie C. Merrill, *Ex-charity Chief Wooed Her Kid Sis*, N.Y. DAILY NEWS (Mar. 10, 1995, 12:00 AM), http://www.nydailynews.com/archives/news/ex-charity-chief-wooed-kid-sis-article-1.684001.

107. *Id.*

108. His obituary indicates he and his wife, Bebe, agreed to separate in 1988 and finalized their divorce in 1991. *See* Robert D. McFadden, *William Aramony, United Way Leader Who Was Jailed for Fraud, Dies at 84*, N.Y. TIMES (Nov. 13, 2011), http://www.nytimes.com/2011/11/14/business/william-aramony-disgraced-leader-of-united-way-dies-at-84.html (summarizing the timeline of William Aramony's marriage to Bebe Ann Nojeim). Other newspaper articles report that between 1986 and 1991, Aramony carried on affairs with Lori Villasor as well as, at least, two other female employees at UWA. *See Charitable Seductions*, TIME, June 24, 2001, http://content.time.com/time/magazine/article/0,9171,162980,00.html; Merrill, *supra* note 106 (recounting the development of the relationship between Aramony and the Villasor sisters).

109. Merrill, *supra* note 106.

110. *Charitable Seductions*, *supra* note 108.

Aramony's confrontation with UWA allegedly began after an anonymous letter was sent to the chairman of UWA's executive committee, on UWA letterhead, demanding Aramony's removal for financial irregularities and other misbehavior at his office.[111] Adverse news reports and media inquiries caused the board to accelerate its investigation out of concern for the impact a public scandal would have on donations to the local groups and voluntary contributions from the local groups to UWA's budget.[112]

For four years, the only action that UWA took against Aramony was self-help.[113] UWA fired Aramony in 1992 (after twenty-two years as the CEO) and canceled his employment contract, claiming his contract and his retirement plans were void.[114] By this time, Aramony and UWA were under investigation by a variety of city, state, and federal government agencies.[115]

While the criminal proceedings continued,[116] Aramony filed a suit in 1996 against UWA to collect compensation under his contract, and more importantly, to establish his retirement benefits.[117] UWA counterclaimed against Aramony for fraud and breach of fiduciary duty.[118] The delay in UWA's assertion of its claims diminished the eventual award of forfeiture and other damages because of the statute of limitations.[119]

It might seem reasonable to expect an easier civil law suit when the defendant has been convicted on fifteen criminal charges[120] that relate to your civil claims, but UWA was somewhat disappointed with the court's

111. *Aramony II*, 28 F. Supp. 2d 147, 161 (S.D.N.Y. 1998), *aff'd in part*, *rev'd in part sub nom. Aramony III*, 191 F.3d 140 (2d Cir. 1999).

112. *See, e.g.*, Charles E. Shepard, *United Way Head Resigns over Spending Habits*, TECH (Boston), Feb. 28, 1992, at 3 (speculating "Aramony might be replaced . . . in an effort to assure that local United Ways make as swift a recovery as possible from a public relations debacle that many feared would hurt their annual fund-raising drives").

113. *See Aramony II*, 28 F. Supp. 2d at 160–61 (discussing UWA's executive committee's attempts to manage public relations following their discovery of Aramony's misconduct).

114. *Id.* at 152–53.

115. *Id.* at 163–64 (identifying numerous state and federal agencies were actively investigating UWA and Aramony).

116. *Aramony III*, 191 F.3d 140, 146 n.2 (2d Cir. 1999) (noting Aramony was convicted of more than twenty counts of fraud, mail fraud, tax fraud, and other related crimes, and he was sentenced to seven years of prison).

117. Aramony v. United Way of Am. (*Aramony I*), 949 F. Supp. 1080, 1082 (S.D.N.Y. 1996).

118. *Aramony II*, 28 F. Supp. 2d at 153.

119. *Id.* at 176.

120. *See id.* at 157–58 (holding, as to the estoppel effect of Aramony's six mail fraud convictions, one wire fraud conviction, and his conviction on eight counts of interstate transportation of fraudulently obtained property).

response to their estoppel motion.[121] The judge generally agreed Aramony should be estopped from denying the acts for which he was convicted, but she limited the estoppel to only those specific criminal acts and not other acts related to civil liability.[122] The facts proven were damning but limited in dollar amount and still subject to the possibility that the board may have waived some or all of Aramony's liability during its negotiations.[123] The only direct evidence of Aramony's disloyalty was the estoppel effect of his criminal convictions and the testimonies of a former secretary and an assistant who described Aramony's process of dictating his expense reports daily over the phone—a process the trial judge later called "creative coding."[124]

UWA's claim for compensatory damages was limited by two further issues. The first issue was that damages were constrained by the seven-year statute of limitations provided under New York law for victims of crime[125] to a remaining period from September 1989 through December 1991.[126] Further, under that statute, UWA's recovery was also limited to the conduct for which Aramony was convicted.[127] The second issue concerned implied waiver. The court held UWA had effectively waived many of Aramony's key criminal acts through the board's attempts to reconcile with Aramony.[128]

The board of director's actions before the lawsuit suggest they were indecisive. For the year prior to his departure, Aramony had a series of increasingly confrontational meetings with the board of directors.[129] The board authorized an extensive investigation by outside counsel, special investigators, accountants, and public relations consultants.[130] Before the board eventually fired him, it passed resolutions of confidence in Aramony twice and once refused to accept his resignation; although, at that time, the board was only partially informed of the true extent of his disloyalties.[131]

121. *See id.* (limiting the application of estoppel to Aramony's criminal convictions).

122. *Id.*

123. *Id.* at 176 n.30.

124. *Id.* at 158–59 (describing the process employed by Aramony to code expense reports stating, "[s]uch 'creative coding' occurred on a monthly basis from 1982 through at least September 1989").

125. N.Y. C.P.L.R. § 213-b (2001).

126. *Aramony II*, 28 F. Supp. 2d at 176.

127. *Id.* at 176 n.29.

128. *Id.* at 176 n.30.

129. *See id.* at 160–61 (describing UWA's executive committee's meetings with Aramony to discuss his misconduct and his offer of resignation).

130. *Id.* at 159.

131. *Id.* at 160–61.

Aramony's claim that UWA waived his liability for his misdeeds, however, proved successful in eliminating his liability for some of the more important actions for which he was convicted.[132]

The *Aramony* case is also noteworthy on three other issues. First, the court did not deny the possibility of awarding consequential damages for the subsequent decline in contributions to the local United Way groups or the groups' pledges of support for UWA. Instead, Judge Scheindlin held UWA's claim for lost contributions,[133] ranging from $12 million to $32 million, was excessively speculative.[134] In light of the judge's ruling on estoppel, UWA would have had to prove how Aramony's criminal actions caused the decline in contributions to the local groups and the decline in the groups' voluntary pledges to UWA.[135] The expert testimony was insufficient to find Aramony's criminal activities and "creative coding" were a substantial cause for the decline in contributions from the local groups.[136]

Second, UWA pursued a wide-ranging investigation into Aramony's activities and their likely impact on UWA and its public image. UWA asserted a claim for the direct costs of the investigation for $2,318,164,[137] which was approved only in the amount of $232,138[138] after applying the substantial factor causation standard.[139] The professional invoices were not properly detailed or itemized by issue to ensure a fair allocation process or one tied to the limited estoppel effect.[140] Furthermore, some

132. *Id.* at 176 n.30.

133. In retrospect, one observer has concluded that the scandal had a significant impact. *See Old Battles and New Challenges*, *supra* note 99 ("Several United Ways disaffiliated themselves with the national office and filed name changes. . . . . The immediate decline of donations to United Ways in 1992 and 1993 followed two years of slowing campaigns amid the economic doldrums of the early 1990s. UW agencies saw smaller allocations.").

134. *Aramony II*, 28 F. Supp. 2d at 178.

135. *See id.* at 177 ("Even assuming that UWA reduced its percentage in response to the withholding of dues in early 1992, Aramony's criminal conduct was not a 'substantial factor' in causing that reduction.").

136. *See id.* ("In an action for breach of fiduciary duty, a party may recover consequential damages without proving that his injury was foreseeable or anticipated; rather, he need only show that the breach was a substantial factor in causing the injury.").

137. *See id.* at 176, 179–81 (detailing UWA's claim for an additional $1,935,699 of indirect, consequential expenses, which were denied).

138. *Id.* at 179–81.

139. *See id.* at 177. The Second Circuit later noted, without ruling, that the substantial factor test may be inappropriate. *Aramony III*, 191 F.3d 140, 154 n.7 (2d Cir. 1999) (noting one court's decision to "reject[] use of 'substantial factor' analysis, in favor of proximate causation, where remedy sought is compensatory damages rather than restitution" (citing LNC Invs., Inc. v. First Fidelity Bank, N.A. New Jersey, 173 F.3d 454, 465 (2d Cir. 1999))).

140. *Aramony II*, 28 F. Supp. 2d at 176, 180.

of the items claimed were not in sync with the estoppel order.[141] For example, UWA claimed more than $127,000 in consequential damages to pay for a headhunter agency to replace Aramony.[142] The court allowed none of that claim because UWA failed to prove how much more expensive it was to replace Aramony because of his criminal activities.[143] In total, all compensatory and consequential damages, other than forfeiture, amounted to only $232,138 (including the $85,400 of investigation and other consequential expenses) plus prejudgment interest of $125,751, based solely on the partial reimbursement for investigation expenses.[144]

The third issue concerns the forfeitability of retirement benefits and a dispute over dueling plans for retirement benefits. UWA contended a draft of the defined benefit plan was the applicable plan even though it was never executed.[145] That draft was important because its felony forfeiture provision provided that the retirement benefits were non-forfeitable unless the beneficiary was convicted of a felony commission of fraud or embezzlement.[146] Aramony prevailed in his assertion that the executed plan controlled and that the plan was therefore non-forfeitable.[147] However, the separate "top hat" plan had no provision relating to forfeitability and was therefore subject to forfeiture, which increased Aramony's loss by about $300,000.[148] For this round of the litigation, UWA was found liable for Aramony's retirement benefits in the amount of $3,221,057 plus prejudgment interest of $1,177,121.[149] The Second Circuit issued two subsequent opinions that reversed the Southern District of New York on parts of this issue; although, Aramony did keep his main retirement benefits.[150]

141. *See id.* at 176, 1881 (denying relief where "Aramony's criminal conduct was not a substantial factor in causing UWA to incur the cost of searching for a new president").

142. *Id.* at 176, 181.

143. *Id.*

144. *Id.* at 182, 185.

145. *Id.* at 153.

146. *Id.* at 155.

147. *Id.* at 166.

148. *Id.* at 171.

149. *Id.* at 175.

150. Aramony v. United Way of Am. (*Aramony IV*), 254 F.3d 403, 405 (2d Cir. 2001) (affirming the trial court's initial findings, except the portion holding United Way "estopped from denying that Aramony was entitled to certain benefits under a Replacement Benefit Plan to replace benefits lost [due to the IRS Code placing] a cap on the annual compensation that can be taken into account by a qualified pension plan" (citation omitted)). The case was remanded, and the district court found Aramony was entitled to replacement benefits; however, on the second appeal, the court reversed and found in favor of United Way, holding Aramony was not entitled to the replacement benefits.

Subject to the advice of an ERISA lawyer, the key issue is not the mechanics of defined benefit plans nor ERISA law but the fact that a non-forfeitability clause could have saved or preserved the top hat plans, which were not protected by ERISA.[151] Only a few cases relating to the forfeitability of top hat plans have been heard, but their dicta confirm this inference.[152] Aside from benefit plans, one other opinion suggests a prior contractual agreement can trump forfeiture.[153] It remains to be seen whether non-forfeitability clauses will be upheld outside of ERISA plans; if so, it seems inevitable that a new CEO employment contract will test public policy with the specific provision that all compensation is agreed to be non-forfeitable, regardless of the employee's subsequent actions.

The amount of Aramony's compensation to be forfeited was not in doubt and not discussed at length.[154] His compensation was held forfeit from September 1989 to December 1991, which was the period of his disloyalty as abridged by the statute of limitations.[155] The sum of forfeited compensation ($951,250), prejudgment interest ($662,805), and the value of the forfeited top hat plan ($300,000), totaling $1,914,055, amounted to 80% of the total award and 535% of compensatory damages ($232,138 plus prejudgment interest of $125,751).[156]

Judge Scheindlin's opinion never clearly reconciles the damage numbers sufficiently to openly state Aramony was not held liable for any of UWA's losses from creative coding or self-dealing.[157] Damages consisted entirely

Id.

151. *See* Bigda v. Fischbach Corp., 898 F. Supp. 1004, 1016 (S.D.N.Y. 1995) ("Since ERISA intentionally omits top hat plans from its nonforfeitability protection, federal common law may not be used to create nonforfeitability protection under ERISA."), *aff'd*, 101 F.3d 108 (2d Cir. 1996).

152. *See* Tyco Int'l, Ltd. v. Kozlowski (*Kozlowski I*), 756 F. Supp. 2d 553, 565 (S.D.N.Y. 2010) ("Under federal common law, benefits accrued in top hat plans are assumed to be forfeitable unless otherwise agreed to by the parties to the contract." (citing *Bigda*, 898 F. Supp. at 1016)); Foley v. Am. Elec. Power, 425 F. Supp. 2d 863, 871 (S.D. Ohio 2006) ("As to the issue of forfeiture, courts have held that if a top hat plan does not contain a non-forfeiture agreement, then an employer may withhold that portion of benefit plan payment that accrued during periods of employee disloyalty.").

153. G.K. Alan Assoc., Inc. v. Lazzari, 840 N.Y.S.2d 378, 385 (App. Div. 2007) ("[T]he 'surrounding circumstances' include the facts that the stock purchase and consulting agreements were both undisputedly executed on the same day and that the terms of the consulting agreement include Lazzari's waiver of any defense to his obligation to make payments under the agreement on the basis of Alan's failure to provide the consulting services required of it."), *aff'd*, 893 N.E.2d 133 (N.Y. 2008).

154. *See Aramony II*, 28 F. Supp. 2d at 171 ("Under the federal common law of forfeiture, which is derived from the consensus approach of state courts, employees cannot recover non-vested pension benefits that accrued during periods of disloyalty.").

155. *Id.* at 176.

156. *Id.* at 172, 185.

157. *See Aramony III*, 191 F.3d 140, 147 (2d Cir. 1999) (detailing amounts pled and awarded for damages from the lower court).

of forfeited compensation and a small portion of UWA's investigation expenses plus prejudgment interest.[158] The judge held UWA had adequately proven Aramony was disloyal and had breached his fiduciary duty sufficiently to warrant full compensation forfeiture; but, other than partially compensating UWA for its investigation expenses, no other damages were approved.[159]

In considering punitive damages, the federal judge made some "hard" statements about Aramony stealing from a public charity and the egregiousness of his actions but still only assessed punitive damages at $50,000.[160] Judge Scheindlin reasoned punitive damages are intended to punish and deter.[161] She concluded Aramony's criminal sentence (a prison term of seventy-eight months (at age sixty-eight) and a fine of $300,000) was sufficient punishment.[162] Accordingly, in recognition of UWA's consequential loss of goodwill, she awarded merely a token amount of punitive damages of $50,000.

Effectively, the punitive damages were greater than the $50,000 awarded in recognition of UWA's consequential loss of goodwill.[163] Judge Scheindlin held New York law provided for prejudgment interest for breach of fiduciary duty at the discretion of the trial judge.[164] Exercising that discretion, she awarded $662,805 of prejudgment interest to compensate UWA for some of the damages that could not be quantified.[165]

Aramony was released in 2001 after serving more than six years of his

158. *Aramony II*, 28 F. Supp. 2d at 185.

159. *Id.* at 184–85.

160. *Id.* at 184.

161. *Id.*

162. *Id.*

163. *Id.* (noting the "wanton and reckless nature of [Aramony's] misconduct exposed the UWA to contempt and ridicule, and angered its most ardent supporters"). The court continues, recognizing the real damage to UWA "cannot be quantified in dollars and cents" and imposing punitive damages "to be sure that those who abuse the public, on whose behalf they supposedly work, are punished and that others in that position are deterred." *Id.*

164. *See id.* at 182 (acknowledging an award of "prejudgment interest in cases involving breach of fiduciary duty . . . is not mandated").

165. *See id.* ("Its award is 'founded on the fact that the aggrieved party has been damaged by a loss of the use of the money or its equivalent and that unless interest is added the party aggrieved is not made whole.'" (quoting Bulk Oil (U.S.A.), Inc. v. Sun Oil Trading Co., 697 F.2d 481, 484–85 (2d Cir. 1983))). For examples of other cases where prejudgment interest was awarded alongside compensation forfeiture, see *V.I.M. Recyclers, LP v. Magner*, No. 03 C 343, 2005 WL 1745657 (N.D. Ill. July 21, 2005), *Dernick Resources, Inc. v. Wilstein*, No. 01-13-00853-CV, 2015 WL 3981772 (Tex. App.—Houston [1st Dist.] 2015, no pet.), and *McCullough v. Scarbrough, Medlin & Associates Inc.*, 435 S.W.3d 871, 884 (Tex. App.—Dallas 2014, pet. denied).

seven-year sentence.[166] He married within the first year of his release and was reported to have been active in the promotion of mutual understanding in the Middle East until his death in 2011 at the age of eighty-four.[167] Indefatigable!

C. *Lars Bildman: He Treated His Company Like a "Personal Checkbook and His Sexual Fiefdom"*[168]

Bildman's former employer, the plaintiff in the suit for breach of fiduciary duty, Astra USA, Inc. (Astra), also discovered that securing a damages award against a convicted fraudfeasor can be difficult despite apparent evidence of about $14 million of losses or damage.[169] Despite the evidence that Bildman wasted at least $3 million of Astra's funds[170] and was responsible for a public scandal that required more than $905,080 in investigation expenses,[171] Astra was awarded only $1,040,812 in compensatory damages at trial.[172] The award of roughly $6.8 million for compensation forfeiture by the Massachusetts Supreme Court[173]—applying New York rather than Massachusetts law—therefore proved instrumental in providing substantial reimbursement.[174] In the last year of his employment, Bildman was paid an annual salary of $944,491 in addition to a supplemental stock grant valued at $203,691.[175]

Lars Bildman reorganized and grew Astra, the U.S. sales operation for a Swedish pharmaceutical company, Astra AB. He built up Astra to a 500-person organization by focusing on the market niche of prescribing doctors.[176] However, his marketing and organizational expertise was countervailed by his pervasive practice of expense fraud and by his

166. *Aramony IV*, 254 F.3d 403, 405 (2d Cir. 2001). *See* McFadden, *supra* note 108 (indicating Aramony was released from prison in September 2001 after being in prison for six years).

167. McFadden, *supra* note 108.

168. Astra USA, Inc. v. Bildman (*Bildman IV*), 914 N.E.2d 36, 51 n.30 (Mass. 2009).

169. *See generally* Astra USA, Inc. v. Bildman (*Bildman III*), Nos. 980580C, 991942G, 2006 WL 760283, at *8 (Mass. Dist. Ct., Super. Ct. Jan. 26, 2006) (showing, despite Bildman's unsavory behavior, the court was unwilling to include all the damages Astra wanted because the behavior could be viewed as part of the corporate culture), *aff'd in part*, *rev'd in part*, 914 N.E.2d 36 (Mass. 2009).

170. *See Bildman IV*, 914 N.E.2d at 43 n.13 (examining Bildman's misuse of Astra's funds).

171. *Bildman III*, 2006 WL 760283, at *8.

172. *Id.* at *1.

173. *See Bildman IV*, 914 N.E.2d at 58 (reversing "the judgment denying Astra recovery of compensation it paid to Bildman during the period of his disloyalty—$5,599,097 in salary and $1,180,000 in bonuses").

174. *See id.* at 50–51 (finding the trial court's "invocation of Massachusetts' doctrines of equitable forfeiture" inappropriate because New York precedent required forfeiture).

175. *Id.* at 40 n.8.

176. *Id.* at 40.

enforcement of an office environment that facilitated sexual predation and harassment for more than ten years.[177] Eventually twelve women claimed they had been harassed by Bildman or some other executive,[178] and evidence was uncovered that over a ten-year period, Bildman (a married man) had paid or authorized payments of hush money to at least five women (departing victims or witnesses), totaling more than $270,000.[179] Four of the payments to his victims were in connection with his former secretary.[180] As a result of the subsequent EEOC investigation, Astra entered into a consent decree that provided a fund of $9,850,000 to compensate the victims.[181]

The report of an impending cover-story article in *Business Week* on sexual harassment at Astra precipitated Bildman's confrontation with Astra AB.[182] Bildman first learned of the tentative *Business Week* article in December 1995 and immediately mobilized a task force of outside attorneys and internal executives to investigate the leaks of information from Astra to *Business Week*.[183] From December 1995 through the following April, Bildman resisted internal inquiries and investigations with denials;[184] he even orchestrated a campaign in which he ordered female

177. *See Bildman III*, 2006 WL 760283, at *1, *5 (noting "Bildman's tenure at Astra USA was highly successful with the exception of the serious matter that gave rise to his termination," which led to a jurying finding Bildman liable to Astra for fraud, conversion, waste of its assets, breach of fiduciary duty to Astra, and sexual harassment of its employees); *see also Bildman IV*, 914 N.E.2d at 40–41 (describing how Bildman, as early as 1985, had authorized and signed an agreement with compensation, in excess of $3,000 per month, for his former secretary who testified she had "left the company after she had been forced to have sexual relations with Bildman").

178. *Bildman IV*, 914 N.E.2d at 43 (commenting on the complaints received about Bildman and other Astra Executives for their sexual harassment (quoting Mark Maremont, *Abuse of Power: The Astonishing Tale of Sexual Harassment at Astra USA*, BUSINESS WEEK, May 13, 1996, at 87)).

179. *See id.* at 40–41 (detailing the payments authorized by Bildman in response to sexual harassment allegations since 1985).

180. *See id.* at 41.

181. The trial judge rejected the company's attempt to include the amount of the consent decree as compensatory or consequential damages. *See* Astra USA, Inc. v. Bildman (*Bildman I*), No. 980580C, 2000 WL 33596823, at *4 (Mass. Dist. Ct., Super. Ct. Dec. 19, 2000) (rejecting Astra's attempt and emphasizing Astra's consent decree arose "from an action against *Astra*, *not Bildman*"). The judge noted Bildman was not present or represented during the EEOC investigation. *See id.* at *4 ("Astra's consent decree with the EEOC focused on its own sexual harassment policies and practices, and the underlying case related to the hostile work environment created by several individuals connected with Astra, not Bildman alone.").

182. *See Bildman IV*, 914 N.E.2d at 41–43 (exploring the sequence of events following the announcement that *Business Week* was going to release an article about the sexual harassment).

183. *See id.* at 41 ("The task force was not set up to investigate the merits of the sexual harassment claims but rather to determine *Business Week*'s sources of information and to control the flow of information to *Business Week* and Astra AB.").

184. *See id.* at 41–42 (examining Bildman's many assurances of Astra's good record to Astra AB

Astra employees "to write letters of support for him to Astra AB."[185]

But despite Bildman's best efforts, rumors of the article finally reached Astra AB leadership, and on April 28, 1996, Bildman was suspended with pay after a preliminary internal investigation.[186] Astra AB thereafter retained outside counsel to conduct a more thorough investigation in which Bildman resisted and refused to assist with any interviews.[187] Against Astra AB's specific request, he and another associate also conducted a campaign of contacting Astra employees to request or threaten them to deny any knowledge of Bildman's sexual harassment.[188] Astra also presented evidence at trial that Bildman's group destroyed documents and erased computer hard drives.[189]

On June 25, 1996, Bildman was fired after Astra AB got the results from the second internal investigation.[190] That report concluded more than $2 million of company funds had been spent on Bildman's personal activities and more than $1 million on falsified expense reimbursements.[191] The report also suggested sexual harassment was ongoing but nothing comparable to that published earlier in the May 1996 *Business Week* cover article, *Abuse of Power: The Astonishing Tale of Sexual Harassment at Astra USA*.[192]

The magazine article not only eliminated any chance for Astra to resolve its issues with Bildman in a private manner, but it also attracted the attention of various governmental agencies, such as the EEOC and the IRS.[193] In March 1997, a federal grand jury indicted Bildman for various forms of fraud.[194] In January of the following year, "he [pled] guilty to three counts of willfully filing false [f]ederal tax returns[,] [and] by plea agreement, the remaining counts were dismissed, including counts

officials).

185. *Id.* at 42 n.11.

186. *Id.* at 42.

187. *See id.* (indicating Bildman, contrary to Astra AB instruction, did not cooperate fully and did not refrain from contacting Astra employees about the investigation).

188. *Id.* at 42–43.

189. *Id.* at 43.

190. *Id.*

191. *Id.* at 43 n.13.

192. *See Bildman IV*, 914 N.E.2d 36, 43 (Mass. 2009) (noting there were "a dozen cases of women who claimed they were either fondled or solicited for sexual favors" (quoting Mark Maremont, *Abuse of Power: The Astonishing Tale of Sexual Harassment at Astra USA*, BUSINESS WEEK, May 13, 1996)).

193. *Id.* at 43 & n.15.

194. *Id.* at 43 n.15.

charging Bildman with defrauding Astra."[195]

In January 2002, Bildman's civil trial commenced and endured for seven weeks.[196] The jury awarded $875,512 in compensatory damages for fraud and conversion and $1,040,812 for both waste of corporate assets and breach of fiduciary duty.[197] However, the jury also found the two awards overlapped and, thus, only the larger sum was actually awarded.[198] And, while the jury did find Bildman had engaged in sexual harassment, no separate damages were awarded.[199] The jury also concluded Astra had not breached the employment agreement by terminating Bildman or by cutting off his participation in the profit sharing plan.[200]

Both the trial court and the state supreme court ruled against including any part of Astra's investigatory expenses of $905,080 as compensatory damages.[201] The supreme court acknowledged such expenses as a possibility for compensatory damages but concluded Astra's efforts failed to prove Bildman's actions were a substantial factor in causing the investigatory expenses.[202]

The trial judge correctly held New York law controlled on the issue of compensation forfeiture as Astra was incorporated in New York.[203] The state supreme court specifically noted Astra was not suing Bildman under the employment agreement that provided Massachusetts law

195. *Id.* at 44 n.15.

196. *Id.* at 44.

197. *Bildman III*, Nos. 980580C, 991942G, 2006 WL 760283, at *1 (Mass. Dist. Ct., Super. Ct. Jan. 26, 2006), *aff'd in part*, *rev'd in part*, 914 N.E.2d 36 (Mass. 2009).

198. *Id.*

199. *Id.* ("[T]he jury found that Bildman breached his fiduciary duty to Astra by making affirmative misrepresentations while he was its President and CEO, failing to disclose material information he had a duty to disclose, and improperly using Astra funds."). Further, they found he "engaged in sexual harassment, violated Astra's sexual harassment policy, and retaliated against one or more Astra employees who exercised their right to make a complaint under Astra's sexual harassment policy." *Id.*; *see also Bildman IV*, 914 N.E.2d at 44 (acknowledging the trial verdict did not provide additional damages upon finding Bildman had engaged in sexual harassment).

200. *Bildman IV*, 914 N.E.2d at 44.

201. *Id.* at 54; *Bildman III*, 2006 WL 760283, at *8 & *10 n.5.

202. *See Bildman IV*, 914 N.E.2d at 52–53 (stating "the 'substantial factor' standard is insufficient to satisfy causation"); *see also Aramony II*, 28 F. Supp. 2d 147, 177–78 (S.D.N.Y. 1998) (examining a trial judge's rejection of the complete inclusion of one type of damage because the defendant's misconduct was not proven as a substantial factor causing that damage), *aff'd in part*, *rev'd in part sub nom. Aramony III*, 191 F.3d 140 (2d Cir. 1999).

203. *See Bildman IV*, 914 N.E.2d at 39 & n.4 (stating Massachusetts applies the law of the company's state of incorporation for matters of internal corporate affairs (citing Harrison v. NetCentric Corp., 744 N.E.2d 622, 628 (2001))); *see also id.* at 50 & n.27 (noting Astra made no claim under the employment contract governed by Massachusetts law).

controlled.[204] Thereafter, the judge erred because, even though she found New York law controlled, she still effectively applied Massachusetts law on compensation forfeiture.[205]

The supreme court held New York law largely requires full forfeiture for cases in which the defendant commits repeated acts of disloyalty.[206] Even if there were some flexibility to this standard, the facts warranted full forfeiture because of Bildman's egregious behavior:

> The evidence heard by the jury was overwhelming that from 1991 through 1996, Bildman used Astra as his personal checkbook and his sexual fiefdom, in the process driving away employees, creating a corrosive corporate atmosphere, causing Astra actual loss, and leading to months of bad publicity about the company. We agree with Astra that, as a matter of law, even under the more lenient substantial and pervasive standards of forfeiture, Bildman's breaches of fiduciary duty mandate equitable forfeiture of his compensation during the period of his disloyalty.[207]

That holding added an award of $6,779,097 (no prejudgment interest) to the $1,040,812 of compensatory damages.[208] If Massachusetts law had controlled, the trial judge would have had sufficient discretion to deny forfeiture.[209]

In her discretion, the trial judge awarded no punitive damages even though Bildman served no jail time.[210] Believing she had discretion to award forfeiture, she also rejected forfeiture of Bildman's compensation as damage overkill.[211] The forfeiture amount represents 650% of the

204. *Id.* at 50 n.27 ("Astra makes no claim of breach of fiduciary duty under the employment agreement, which is governed by Massachusetts law. Its claim for forfeiture is explicitly (and exclusively) based on loyalty principles.").

205. *See id.* at 50–51 (summarizing the trial court judge's "invocation of Massachusetts doctrines of equitable forfeiture" as inappropriate because it was contrary to New York precedent).

206. *Id.* at 51; *see id.* at 47 ("The court held that where 'defendants engaged in repeated acts of disloyalty, complete and permanent forfeiture of compensation, deferred or otherwise, is warranted under the faithless servant doctrine.'" (quoting William Floyd Union Free Sch. Dist. v. Wright, 877 N.Y.S.2d 395, 397 (App. Div. 2009))).

207. *Id.* at 51 n.30 (citation omitted). The court also notes, under New York law, the value of Bildman's services was irrelevant. *Id.* at 50.

208. *See id.* at 58 (reversing the trial court's decision to deny Astra of the compensation it paid Bildman during his disloyalty).

209. *See id.* at 50 (emphasizing the trial court's inappropriate use of Massachusetts equity law).

210. Astra USA, Inc. v. Bildman (*Bildman II*), Nos. 980580C, 981942C, 2005 WL 6190792, at *14 (Mass. Dist. Ct., Super. Ct. May 4, 2005), *aff'd in part*, *rev'd in part*, 914 N.E.2d 36 (Mass. 2009).

211. *See Bildman III*, Nos. 980580C, 991942G, 2006 WL 760283, at *9 (Mass. Dist. Ct., Super. Ct. Jan. 26, 2006) (concluding Astra, in the court's discretion, was not entitled to compensation forfeiture because it would impose a disproportionately harsh penalty), *aff'd in part*, *rev'd in part*, 914 N.E.2d 36 (Mass. 2009).

compensatory damages. It is surprising that Astra secured such a small relative amount of damages for its losses of $2 million wasted on personal uses, $1 million of expense fraud, $250,000 of hush money, and $905,080 in investigation costs. Astra also failed to secure an award of damages related to the harassment or the EEOC settlement fund.[212] Part of the answer lies in the trial judge's perception that some of Bildman's misbehavior was the result of Astra AB's corporate culture and tolerance.[213]

The trial judge's opinion contradicts the perception that the scale and nature of egregiousness of the fiduciary's breach will necessarily affect the outcome of the claim. There was ample evidence of Bildman's disloyalty, the resulting damage and loss to the employer, and spoliation of evidence.[214]

D. *Ian Gittlitz: Remedy Overkill*

In a four-day trial, Ian Gittlitz's employer, ICD Publications, Inc. (ICD), was awarded all damages that it sought: all compensatory damages, full compensation forfeiture, and $2 million of punitive damages.[215] Equally significant, Gittlitz's co-shareholders exercised their right to purchase his stock at book value.[216] The resulting combination seems sure to have caused Gittlitz's financial ruin.

Ian Gittlitz founded ICD in 1989 with two equal shareholders, Cyndi Evans and David Palcek, who had worked together since at least 1987.[217] ICD produced trade publications for the home housewares industry. Gittlitz operated as president of the company out of the Long Island office while Evans and Palcek worked in the Lincolnshire office in Illinois.[218] Apparently the company was highly profitable because Gittlitz's compensation between 2000 and 2007 was $6,021,657, which closely reflects his one-third share of the three owners' total compensation.[219] Gittlitz's wife was also employed in the Long Island

212. *Id.* at *8.

213. *See id.* ("Here, Bildman's breach of fiduciary duty constitutes serious misconduct. In weighing the equities, however, this court considers that some of Bildman's unsavory behavior may have been in keeping with Astra's corporate culture at the time in question, and tolerated, at least for a time, by the directors.").

214. *Bildman IV*, 914 N.E.2d at 43.

215. ICD Publ'ns, Inc. v. Gittlitz, 2014 IL App (1st) 133277, ¶¶ 42–43.

216. *See id.* ¶ 31 (ordering specific performance for Gittlitz to transfer his stocks at book value).

217. *Id.* ¶ 3.

218. *Id.* ¶¶ 3–4.

219. *Id.* ¶ 34.

office as the administrative manager.[220]

Despite receiving average annual compensation of almost $1 million, Gittlitz actively defrauded his company in a pattern of expense fraud and unauthorized advances.[221] He and his wife had sole access to ICD's checkbook, bank accounts, and credit card records, so he was free to double charge invoices for expenses and use the receipts and invoices of other employees to support false expense reports.[222] He also took advances for himself from company funds that he never repaid.[223]

Early in 2007, Evans and Palcek began to question the accuracy of Gittlitz's expense reports.[224] After they confirmed at least some of his reports were false, they confronted Gittlitz on May 7, 2007, and he admitted to a temporary lapse in a small amount.[225] The three shareholders signed a letter agreement titled "ICD Publications Change of Financial Controls" (CFC Agreement),[226] which reformed the accounting and financial controls as well as retired his wife from her administrative position.[227]

The outside auditor, who was subsequently retained, quickly discovered Gittlitz had forged a board resolution and other documents to enhance his financial control over the company accounts.[228] The auditor also determined Gittlitz had advanced himself $80,000 in March 2007 and more than $1 million since 2000.[229]

Evans and Palcek fired Gittlitz on June 21, 2007, and on July 10, 2007, they purchased his stock. The shareholder agreement provided the shares

220. *Id.* ¶ 4.

221. *Id.* ¶¶ 5–6.

222. *Id.* ¶ 4.

223. *Id.* ¶ 6.

224. *Id.* ¶ 7.

225. ICD Publ'ns, Inc. v. Gittlitz, 2014 IL App (1st) 133277, ¶¶ 14–15 ("Evans testified: 'Ian convinced us at that moment that this was a short period of time, was a limited amount of money.' Although Gittlitz admitted to submitting invalid expense reports at that meeting, he did not disclose to Evans or Palcek that he had also been embezzling from ICD by writing him-self 'advance' checks for many years.").

226. *Id.* ¶ 11. Notably, "under the heading 'Confidentiality,' the document stated that: 'Cyndi [Evans] and Dave [Palcek] agree not to seek legal remedies, either criminally or civilly, nor involve the IRS in any findings as it specifically relates to the misuse of company funds provided restitution is made.'" *Id.* ¶ 13.

227. *Id.* ¶ 12.

228. *Id.* ¶¶ 17–18 (detailing ICD's bank file, which included "a purported account signature card that falsely listed Ellen Gittlitz, rather than Evans, as the corporate secretary . . . [and showed] that Evans and Palcek had been removed as signatories on ICD's bank account . . . [and that] the file contained a fraudulent ICD corporate resolution").

229. *Id.* ¶ 19.

were to be purchased at their book value.[230] If, as seems likely, ICD was typical of other companies with large amounts of cash flow and small capital requirements, ICD's book value would understate the fair market value of the shares.

In 2009, Gittlitz was arrested and indicted for theft against ICD and pled guilty to one count of class-3 felony mail fraud for mailing fraudulent expense reports.[231] He specifically acknowledged his fraud between October 2001 through June 2007 (sixty-nine months) and made restitution of $250,000.[232]

The civil case followed a familiar pattern. ICD's motion for summary judgment on Gittlitz's liability was granted in July 2012.[233] The trial to determine damages began on July 22, 2013, during which ICD's expert testified that he found fraudulent transactions from 2000 through 2007 amounting to $1,220,623.[234] Gittlitz did not contest the opposing expert's numbers but instead asserted Evans and Palcek had released him from liability through the CFC Agreement.[235] The court ruled, even if there had been a waiver, it was voidable because it was based on the misrepresentation that Gittlitz's transgressions were relatively small in amount and scope.[236]

Compensation forfeiture in Illinois is expected to result in full forfeiture against a fiduciary that is found liable for substantial disloyalty, but case opinions also emphasize that trial judges should practice discretion.[237] In this case, the trial court awarded full forfeiture over the period of disloyalty, which was confirmed on appeal.[238] The package of remedies

230. *Id.* ¶ 22.

231. *Id.* ¶ 27.

232. *Id.*

233. *Id.* ¶ 30.

234. *Id.* ¶¶ 31–34.

235. ICD Publ'ns, Inc. v. Gittlitz, 2014 IL App (1st) 133277, ¶¶ 36, 44. Despite Gittliz's decision to not contest the opposing expert, the trial judge described his overall attitude as evasive. *Id.* ¶ 89. Gittlitz even attempted to blame the trial court's assessment of his credibility on his stroke, which he claimed affected his speech and recollection, but the appellate court did not buy this excuse. *Id.* ("[T]here is no indication that any speech or medical condition precluded him from testifying coherently or affected the court's assessment of his lack of credibility. To the contrary, the trial transcript confirms that Gittlitz repeatedly offered evasive responses before admitting to the extent of his misconduct.").

236. *Id.* ¶ 44.

237. *See In re* Marriage of Pagano, 607 N.E.2d 1242, 1249–50 (Ill. 1992) (holding the court has discretion to award the appropriate remedy for breaching a fiduciary duty).

238. *Gittlitz*, 2014 IL App. (1st) 133277, ¶ 58 ("In this case, we cannot find error in the court's determination that Gittlitz's breach was willful and deliberate, warranting complete forfeiture of compensation. . . . [T]he trial court was well within its equitable discretion.").

included compensatory damages of $1,220,623 (plus interest of $549,560), forfeiture of $6,021,657 (without prejudgment interest), and punitive damages of $2 million.[239] It seems doubtful that the book value of his stock would be sufficient to offset this judgment totaling $9,791,840.

This case raises two technical issues that were not covered in the appellate opinion. First, in small or closely held companies, tax issues frequently cloud the boundary between salary and distributions of profit to ownership. Sometimes profits are disguised as compensation to avoid double taxation on dividends; but in other cases, compensation is disguised as profits to avoid Social Security and Medicare taxes.[240] It would have been reasonable to assert that a substantial share of his salary was really his one-third share of the profits and that distributions of profit as returns on capital are not subject to forfeiture under any of the supporting rationale.

The second issue relates to the fact that one-third of the money that Gittlitz stole belonged to him as a shareholder; yet, the measure of the damages to ICD failed to adjust for this factor. His share of the damages award did not accrue to his benefit because he was forced to sell his stock after his termination and before the trial.[241] His fellow shareholders could argue that when they bought his stock, they also acquired his interest in the company's chose in action, except, the formula for the purchase price made no allowance for such an adjustment. Sitting in equity, the trial judge was entitled to stress substance over form and could have dismissed that argument or weighed the issue when considering punitive damages or apportionment in forfeiture.[242]

Of the four cases, the result in *Gittlitz* is the most troubling because the total amount of damages seems to exceed the level of punishment normally allowed even for exemplary damages. For stealing $1.2 million, the defendant was ordered to pay a penalty of more than $8 million (an

239. *Id.* ¶¶ 42–43.

240. *See* 1 JAMES O'BRIEN ET AL., THE COMPREHENSIVE GUIDE TO LOST PROFITS AND OTHER COMMERCIAL DAMAGES 230 (Nancy Fannon & Jonathan M. Dunitz eds., 3rd ed. 2014) ("These cases appear to turn on the finding that in a small, closely held business especially, the owner's salary can vary from year to year and does not necessarily correspond to the value of the owner's services." (citing Springs Window Fashions Div., Inc. v. Blind Maker, Inc., 184 S.W.3d 840 (Tex. App.—Austin 2006, pet. granted, judgm't vacated w.r.m.))); *see also* Bettius & Sanderson, PC v. Nat'l Union Fire Ins., 839 F.2d 1009, 1013 (4th Cir. 1988) (stating corporations want to distribute profits "in order to avoid having income taxes imposed twice on what is in reality the same group of people").

241. *Gittlitz*, 2014 IL App. (1st) 133277, ¶ 22.

242. *Id.* ¶ 53 (affirming, in breach of fiduciary cases, "the appropriate remedy is within the equitable discretion of the court" (quoting *In re Pagano*, 607 N.E.2d at 1249–50)).

additional 667%) and was forced to sell his stock at a large discount.[243]

Of the four defendants, Gittlitz's refusal to attempt to reconcile with his partners in May 2007 also seems the most incomprehensible. His fraud, especially the unauthorized draws, was certain to be discovered, and his wife was similarly vulnerable to criminal liability.[244] By negotiating with partners on the basis of full disclosure, he might have avoided $8 million of additional liability and might have been able to reconcile or at least achieve a better salvage value for his stock.

In a famous guest editorial, Alan Dershowitz accused Martha Stewart's lawyers of incompetence because the crimes for which she served time were committed in their presence.[245] Perhaps, Professor Dershowitz overlooked the possibility that she was too irrational at the time to follow the good advice provided by her lawyers—a theory seemingly suggested by these four defendants, especially Gittlitz. Each outlaw failed to attempt an honest reconciliation when offered the chance; they continued to stonewall their way past admissions of felonies and tried to bluster their way past the jury or judge to their inevitable ruin.

E. *Dennis Kozlowski: Number Four on Time's Top Ten Crooked CEOs*

In terms of egregiousness, the outlaws, Grassgreen, Aramony, Bildman, and Gittlitz are not in the same league as Dennis Kozlowski of Tyco International, Ltd. (Tyco) or Richard Scrushy of HealthSouth, Corp. (Scrushy is discussed in Section V). Kozlowski is currently ranked number four on *Time*'s list of the *Top 10 Crooked CEOs* for his crimes and torts while CEO of Tyco.[246] Kozlowski would be the leading outlaw in this Article but for a contradictory case opinion in 2012 from Judge Griesa, a federal district judge in the Southern District of New York that presided over the Tyco cases, which suggests his misgivings about Kozlowski's liability for forfeiture.

243. *Id.* ¶ 42.

244. *Id.* ¶¶ 4, 12 (noting Gittlitz's wife worked alongside him in the New York office until the CFC agreement forced her out).

245. *See* Alan M. Dershowitz, *With Lawyers Like These . . .* , WALL ST. J. (Mar. 8, 2004, 12:01 AM), http://www.wsj.com/articles/SB107870400584448731 (explaining most criminal defendants get a lawyer after committing a crime, but the *Stewart* case seems intriguing because "virtually every action for which Ms. Stewart was convicted took place after she had consulted with highly experienced and expensive lawyers").

246. *Top 10 Crooked CEOs*, TIME, http://content.time.com/time/specials/packages/article/0,28804,1903155_1903156_1903152,00.html (last visited Dec. 11, 2015). He stands behind Bernie Madoff (first) and Ken Lay and Jeffrey Skilling (tied for second and third). *Id.*

Dennis Kozlowski joined Tyco in 1975 as director of internal audit,[247] and he rose to the office of CEO and chairman of the board in 1993.[248] In June 2002 he was fired for cause due to his imminent indictment in New York for sales tax evasion.[249] That indictment led to a broader criminal investigation and a trial in 2005 in which he was convicted on twenty-two of the twenty-three counts and sentenced to prison.[250]

In the criminal trial, Kozlowski was convicted on "[twelve] counts of grand larceny" in the first degree (the value of the property taken for each count exceeded $1 million, and altogether he was held jointly liable for the theft of more than $100 million), "one count of conspiracy to commit larceny, nine counts of falsifying business records, and one count under" the state statute for securities fraud.[251] One of the convictions for falsifying business records arose from his efforts to steal money from Tyco under the company's New York City Headquarters Relocation Loan Program, and the remaining eight arose through his active concealment of unauthorized borrowings from Tyco.[252]

In his 2010 opinion, Judge Griesa granted Tyco's motion for partial summary judgment on the issue of liability for breach of fiduciary duty, inducing breach of fiduciary duty, conspiring to breach fiduciary duty, breach of contract (loan agreements between Tyco and Kozlowski), and conversion.[253] The judge denied Tyco's summary judgment motion on liability for fraud and constructive fraud, as well as equitable claims for accounting, constructive trust, and unjust enrichment.[254]

However, he did grant Tyco's motion for a declaratory judgment to the effect that the retention agreement with Kozlowski was invalid.[255] And since the judge found Kozlowski's disloyalty began no later than September 1995 and continued until his dismissal in June 2002, he held two other compensation and benefit agreements that were executed after September 1995 were also invalid, owing to the CEO's failure to disclose

247. *Kozlowski I*, 756 F. Supp. 2d 553, 555 (S.D.N.Y. 2010).

248. *Id.*

249. *Id.* at 556.

250. *Id.* at 555–56.

251. *Id.* at 556–57.

252. *Id.* at 557.

253. *Id.* at 561–62.

254. *Id.* at 562 ("Tyco brings equitable claims of accounting[,] . . . constructive trust[,] . . . and unjust enrichment . . . . Because questions remain as to whether Tyco's claims for damages will be an adequate legal remedy, Tyco's application for summary judgment as to these equitable causes of action is denied.").

255. *Id.* at 562–63.

his breaches of fiduciary duty.[256]

The judge addressed compensation forfeiture as the "faithless servant doctrine" on a number of points.[257] He found substantial evidence of Kozlowski's disloyalty: after Kozlowski was indicted for sales tax evasion, "[a]n ensuing investigation revealed that Kozlowski had conspired with other corporate officers to pilfer Tyco's treasury of tens of millions of dollars."[258]

Kozlowski's convictions on twelve counts of grand larceny and eight counts of falsification of business records constituted jury findings that he misappropriated property of Tyco with the intent to do wrong and deceive.[259] On the basis of this and other evidence, the judge initially concluded Kozlowski must forfeit all compensation and benefits.[260] Continuing, the judge held Kozlowski must forfeit benefits that accrued under his top hat benefit plans during the disloyalty period.[261] Finally, he held Kozlowski must forfeit all compensation earned during the period of disloyalty spanning from September 1995 until he was dismissed from Tyco in June 2002.[262]

In 2012, Judge Griesa issued a contradictory opinion relating to another motion from Tyco for partial summary judgment for disgorgement of compensation.[263] The judge explained the turnaround as being possible due to an incomplete summary judgment motion: "[T]he application of the faithless servant doctrine was not really closed out in the December 1, 2010 opinion[] because there were no findings as to actual amounts of compensation or actual sums of money."[264] However, this contradicts his previous statement in the 2010 opinion, which declared Kozlowski must

256. *Id.* at 563 ("Because Kozlowski failed to disclose his many breaches of fiduciary duty to Tyco, these contracts were fraudulently induced and are therefore voidable by Tyco.").

257. *Kozlowski I*, 756 F. Supp. 2d 553, 562–63 (S.D.N.Y. 2010) ("A faithless servant is one who owes a duty of fidelity to a principal and who is faithless in performance of his services.").

258. *Id.* at 556.

259. *Id.* at 561.

260. *See id.* at 564 (noting Kozlowski would have to "forfeit all compensation and benefits, deferred or otherwise, earned during his period of disloyalty" because the "multiple breaches of his fiduciary duty over several years clearly demonstrate his faithless service").

261. *Id.* at 565.

262. *Id.* at 562.

263. *See* Tyco Int'l, Ltd. v. Kozlowski (*Kozlowski II*), No. 02 Civ. 7317(TPG), 2012 WL 763553, at *2 (S.D.N.Y. Mar. 9, 2012) (denying Tyco's motion for partial summary judgment based on submissions indicating the parties and the lower court failed to make "a thorough review of the issues relevant to the faithless servant doctrine in connection with the earlier motion, and that the general statements about the doctrine in the December 1, 2010[,] opinion do not deal with certain specific issues which the court is obligated to deal with").

264. *Id.* at *2.

forfeit all compensation earned from September 1995 to June 2002.[265]

Basically, the judge changed his mind about granting summary judgment on compensation forfeiture but not on the breach of fiduciary duty.[266] He raised two factors that were not addressed in the earlier opinion. First, Kozlowski asserted the faithless servant doctrine only applies when the disloyalty "permeated the employee's service in its most material and substantial part."[267] Second, Kozlowski raised the issue of waiver with a citation to the *Aramony* cases. The court thus held Tyco's claim for compensation forfeiture would have to be resolved as questions of triable fact.[268]

Therefore, Dennis Kozlowski's contribution to the law of compensation forfeiture is yet to be determined, and his ranking among fellow outlaws must be deferred. At present, in light of the evidence that Judge Griesa recounted, as well as the colorful egregiousness reported by the media,[269] it seems hard to imagine how Kozlowski can prove that his disloyalty did not materially permeate his service. A holding for less than full forfeiture against a CEO with twenty related convictions would displace the existing belief that New York law requires total forfeiture for substantial disloyalty.[270]

III. BREACH OF FIDUCIARY DUTY

The cases discussed in Section II are not necessarily typical, but they demonstrate some of the issues that regularly appear in these types of cases and reveal the wide combination of remedies applicable to a breach of fiduciary duty claim. They also demonstrate how the cause of action for

265. *Compare Kozlowski I*, 756 F. Supp. 2d at 564 ("Kozlowski must therefore forfeit all compensation and benefits, deferred or otherwise, earned during his period of disloyalty, which began at its latest in September 1995."), *with Kozlowski II*, 2012 WL 763553, at *1–2 (claiming the issue of the faithless service doctrine was not settled in the 2010 case).

266. *See Kozlowski II*, 2012 WL 763553, at *1 (noting the amount of forfeiture was yet to be determined but acknowledging there was a breach of fiduciary duty).

267. *Id.* at *2 (quoting Sanders v. Madison Square Garden, LP, No. 06 Civ. 589(GEL), 2007 WL 1933933, at *3 (S.D.N.Y. July 2, 2007)).

268. *Id.*

269. *See generally Top 10 Crooked CEOs*, *supra* note 246 (describing Kozlowski's "lavish lifestyle").

270. One new piece of evidence recounted in the second opinion relates to the fact that Kozlowski had made restitution to Tyco for $97 million. *See Kozlowski II*, 2012 WL 763553, at *1 ("It should be noted at this point that Kozlowski has already made restitution to Tyco of amounts actually taken from Tyco. The amount of this restitution is approximately $97 million."). Judge Griesa made no mention of whether this restitution represented full restitution or was paid pursuant to some settlement agreement with Tyco nor did he indicate how, if at all, this new fact might adjust any legal issues. *See id.* (failing to examine the reason for the restitution paid to Tyco).

breach of fiduciary duty can lead to stacked remedies: Enstar secured six remedies against Grassgreen,[271] UWA and ICN secured three against Aramony[272] and Gittlitz,[273] and Astra secured two remedies against Bildman.[274]

A. *Dual Goals and Stacked Remedies*

The dual goals[275] for breach of fiduciary duty are (1) to compensate the principal for loss or damages,[276] and (2) to deter further disloyalty by disgorging any profit related to the breach.[277] To satisfy both goals, a remedy in equity and a remedy at law will generally be required. Combining two remedies for one claim of breach of fiduciary duty is commonplace,[278] and combinations of three or more are not unusual in

271. *See* Enstar Grp., Inc. v. Grassgreen, 812 F. Supp. 1562, 1575–76, 1582–84 (M.D. Ala. 1993) (awarding the following claims: forfeiture and recovery of compensation, the profit he made through THL industries, his interest in Macpherson Partners, a prejudgment interest, punitive damages, and the Mendel settlement).

272. *See Aramony II*, 28 F. Supp. 2d 147, 185 (S.D.N.Y. 1998) (concluding Aramony needed to forfeit three years of salary, consequential damages, prejudgment interest, and punitive damages), *aff'd in part*, *rev'd in part sub nom. Aramony III*, 191 F.3d 140 (2d Cir. 1999).

273. *See* ICD Publ'ns, Inc. v. Gittlitz, 2014 IL App (1st) 133277, ¶¶ 58–59 (asserting Gittlitz must forfeit his compensation and pay punitive damages and restitution).

274. *See Bildman IV*, 914 N.E.2d 36, 58 (Mass. 2009) (affirming the judgments against Bildman in regard to attorney's fees and libel, and awarding compensation forfeiture to Astra).

275. *See* Rash v. J.V. Intermediate, Ltd., 498 F.3d 1201, 1212 (10th Cir. 2007) ("Forfeiture is based on two propositions: (1) the principal is considered not to have received what he bargained for if the agent breaches his fiduciary duties while representing the principal, and (2) fee forfeiture is designed to discourage agents from being disloyal to their principal or 'to protect relationships of trust by discouraging agents' disloyalty." (citation omitted)). The court in *Hendry v. Pelland* discusses the dual goals in the context of the lawyer–client fiduciary relationship:

> Compensatory damages make plaintiffs whole for the harms that they have suffered as a result of defendants' actions. Forfeiture of legal fees serves several different purposes. It deters attorney misconduct, a goal worth furthering regardless of whether a particular client has been harmed. It also fulfills a longstanding and fundamental principle of equity—that fiduciaries should not profit from their disloyalty.

Hendry v. Pelland, 73 F.3d 397, 402 (D.C. Cir. 1996) (citation omitted).

276. *See* DOUGLAS LAYCOCK, MODERN AMERICAN REMEDIES 15 (Aspen Publishers, 4th ed. 2010) ("[T]he fundamental principle of damages is to restore the injured party as nearly as possible to the position he would have been in but for the wrong—is the essence of compensatory damages.").

277. *See* RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 43 cmt. b (AM. LAW INST. 2011) ("The basic determination that opens the way to restitution within the rule of this section is always the same: that there has been trust and confidence justifiably reposed on one side, and an advantage improperly gained on the other, either in violation of fiduciary duty or in circumstances posing so great a risk of violation that violation is presumed as a matter of law. Any such advantage must be given up to the beneficiary.").

278. *See* Shaeffer v. Blair, 149 U.S. 248, 258 (1893) (concluding the plaintiff was entitled to receive compensatory damages in the form of reimbursement of his expenditures and was to be

packages that include forfeiture or punitive damages.[279]

The combination of a remedy in equity and a remedy at law tends to resemble a stack of one remedy piled on another rather than two remedies that fit or mesh together because the merger of courts at law and courts in equity has not merged the substance of the two bodies of law. By 1873, the majority of American states had adopted a version of the Field Code, which merged the two court systems.[280] The resulting merger consolidated courtrooms and court personnel, but there has been little progress in reweaving the two bodies of substantive law.[281]

The two goals are related, but they differ: the goal of compensatory damages is to restore the claimant to her ex ante position; the goal of disgorgement is to restore the defendant to her ex ante position by

denied previously agreed commissions); Phansalkar v. Andersen Weinroth & Co., 344 F.3d 184, 204 (2d Cir. 2003) (per curiam) (awarding secret profit and forfeiture); Moore & Co. v. T-A-L-L, Inc., 792 P.2d 794, 800 n.8 (Colo. 1990) (stating, in a failure to disclose case, if "a real estate broker's breach of fiduciary duty causes actual loss to the seller, the broker not only forfeits the commission but also is liable for the full amount of the loss"); Henderson v. Rep Tech, Inc., 557 N.Y.S.2d 224, 225 (App. Div. 1990) (awarding injunctive relief and forfeiture for breach of the principal's confidentiality); Efird v. Clinic of Plastic & Reconstructive Surgery, PA, 147 S.W.3d 208, 221–24 (Tenn. Ct. App. 2003) (holding the defendant was terminated for cause, thereby reversing the employer's liability for compensation under the employment agreement and remanding the case to determine if the defendant was either an officer or director of the employer, which would determine his liability for disloyalty and damages from disloyal competition); V & E Med. Imaging Servs., Inc., v. Birgh, No. 62912-3-I, 2010 WL 4402333, at *7 (Wash. Ct. App. Nov. 8, 2010) (awarding actual damages and forfeiture for fiduciary's conflict); *see also* JOSEPH STORY, COMMENTARIES ON THE LAW OF AGENCY 408 (Bos., Little, Brown & Co., 9th. ed. 1882) ("If, therefore, the agent does not perform his appropriate duties, or if he is guilty of gross negligence, or gross misconduct, or gross unskillfulness[] in the business of his agency, he will not only become liable to his principal for any damages, which he may sustain thereby, but he will also forfeit all his commissions.").

279. For examples of cases in which the court stacked remedies against the defendant for breach of fiduciary duty, see *infra* App. 1.

280. *See* Thomas O. Main, *Traditional Equity and Contemporary Procedure*, 78 WASH. L. REV. 429, 431–32, 464–65 (2003) (exploring why American and English courts unified courts of equity and courts of law into a singular entity).

281. *See* Rogers v. Daniel Oil & Royalty Co., 110 S.W.2d 891, 894 (Tex. 1937) ("In spite of this blended system of law and equity the distinction between them is as absolute as ever, and to entitle the plaintiff to equitable relief he must show a proper case for a court of equity to exercise its equitable jurisdiction." (citing 1 TEX. JUR. *Actions* § 6 (1929))); *see also* Ochoa v. Am. Oil Co., 338 F. Supp. 914, 920 (S.D. Tex. 1972) ("Although the equity side and the law side of the federal trial courts were thus fused, we are still far from the time . . . 'when lawyers will cease to inquire whether a given rule be a rule of equity or a rule of common law.'" (quoting F.W. MAITLAND, EQUITY: A COURSE OF LECTURES 20 (A.H. Chaytor & W.J. Whittaker eds., 1936))); DOMINIC O'SULLIVAN ET AL., THE LAW OF RESCISSION § 10.04 (2008) (stating British fusion did not substantially combine the substance of either body of law); Main, *supra* note 280, at 476 ("As with the Field Code and the Federal Rules of Civil Procedure, the Judicature Acts of 1873 and 1875[] fused only the procedure of law and equity, leaving the substance of equity both intact and predominant . . . .").

transferring unjust enrichment from the defendant to the principal.[282] Only rescission can accomplish both goals in one remedy. Also, neither remedy is dynamic or takes into account the effect of the other: when compensatory damages and forfeiture are combined, the claimant's loss is not adjusted for the effect of disgorging the defendant's unjust enrichment nor is the disgorgement measured by adjusting the defendant's unjust enrichment for the obligation to pay damages to the claimant. Perhaps the lack of such adjustments can be explained by the fact that it is otherwise unusual for compensatory damages and disgorgement to be awarded together.[283]

Equally important is that a merged court has the authority to stack remedies from the two court systems but without many of the constraints that limit such remedies in their native court system.[284] Remedies in equity are constrained by the principle that an accounting in equity, constructive trust, and disgorgement are limited to the defendant's profits, and the defendant is entitled to prove counter-restitution to limit the measure to net profit.[285] The Supreme Court has explained that this principle ensures the exemplary nature of disgorgement is kept in proportion to the defendant's gain.[286] Subsections IV.E and V.B show that forfeiture sometimes avoids this limitation. Furthermore, the law in equity originally did not support punitive damages;[287] it promoted

282. Colleen P. Murphy, *Misclassifying Monetary Restitution*, 55 SMU L. REV. 1577, 1625 n.265 (2002) ("Restitution aims at the defendant's [rightful position]. Disgorgement is the key concept. By making the defendant disgorge the benefits he cannot justly retain, the law of restitution returns the defendant to the position he should, "in equity and good conscience,' have occupied." (alteration in original) (quoting DAVID SCHOENBROD ET AL., REMEDIES: PUBLIC AND PRIVATE 727 (3d ed. 2002))).

283. *See* RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 42, cmt. d (AM. LAW INST. 2011) (stating the award of compensatory damages and disgorgement would be "anomalous in restitution terms, constituting a punitive sanction"); Rendleman, *supra* note 75, at 981 (stating compensatory damages and restitution are mutually exclusive and frequently left to the choice of the plaintiff).

284. Rendleman, *supra* note 75, at 1003 ("Because of the merger of Law and Equity, courts lowered the barriers that previously restricted punitive damages to the common law court and excluded them from Chancery.").

285. Roach, *supra* note 78, at 1291–97 (arguing the law in equity generally requires the measure of unjust enrichment to offset reasonable expenditures that benefit the plaintiff).

286. *See* Snepp v. United States, 444 U.S. 507, 515–16 (1980) (per curiam) (explaining constructive trust remedies "conform[] relief to the dimensions of the wrong. . . . [S]ince the remedy reaches only funds attributable to the breach, it cannot saddle the [fiduciary] with exemplary damages out of all proportion to his gain").

287. *See* Mertens v. Hewitt Assocs., 508 U.S. 248, 270 (1993) ("As this Court has long recognized, courts of equity would not . . . enforce penalties or award punitive damages. . . . [T]his limitation on equitable relief applied in the trust context as well, where plaintiffs could recover

deterrence by disgorging any unjust profits from the defendant even when windfalls to the plaintiff were likely.[288]

The amount of punitive damages awarded by either a court at law or in equity is supposed to be constrained in relation to the amount of actual damages;[289] yet, none of the cases in Section II that considered punitive damages mentioned the simultaneous award of disgorgement or forfeiture as a consideration.[290] In those four cases, the ratio of compensation forfeiture and punitive damages to all other damages was an average of

compensatory monetary relief for a breach of trust, but not punitive or exemplary damages." (citations omitted)); Tull v. United States, 481 U.S. 412, 422 (1987) ("A civil penalty was a type of remedy at common law that could only be enforced in courts of law. Remedies intended to punish culpable individuals, as opposed to those intended simply to extract compensation or restore the status quo, were issued by courts of law, not . . . equity." (citing Curtis v. Loether, 415 U.S. 189, 197 (1974))); Beals v. Wash. Int'l, Inc., 386 A.2d 1156, 1159 (Del. Ch. 1978) (stating the "court of conscience" avoids "vengeance," and punitive "damages are absolutely forbidden in the well-established equity practice"). *But see* RESTITUTION & UNJUST ENRICHMENT § 42 cmt. i ("There are instances of wrongdoing in which the law of restitution imposes [a punitive element of damages].").

288. *See* Randall v. Loftsgaarden, 478 U.S. 647, 663–64 (1986) (acknowledging the remedy in equity "clearly does more than simply make the plaintiff whole for the economic loss proximately caused by the buyer's fraud" and noting such a windfall plays a significant part in deterring the fraudulent party in the realm of securities law (citing Janigan v. Taylor, 344 F.2d 781, 786 (1st Cir. 1965))); Mishawaka Rubber & Woolen Mfg. Co. v. S.S. Kresge Co., 316 U.S. 203, 206–07 (1942) (asserting it is the infringer's burden "to prove that his infringement had no cash value in sales made by him," and "where it is impossible to isolate the profits [that] are attributable to the use of the infringing mark," the trademark owner may receive a windfall on any sales bearing the infringing mark (citation omitted)); Lee v. Lee, 47 S.W.3d 767, 780 (Tex. App.—Houston [14th Dist.] 2001, pet. denied) ("Under the facts of this case, it is more appropriate for the estate to obtain the benefit of a windfall than to let appellee keep $1.5 million in fees the jury found was unreasonable.").

289. In *State Farm Mutual Automobile Insurance v. Campbell*, the Supreme Court refused to hand down a bright-line rule for limiting punitive damages while suggesting, under normal conditions, the ratio should be about four-to-one, or less, subject to the following considerations:

> Nonetheless, because there are no rigid benchmarks that a punitive damages award may not surpass, ratios greater than those we have previously upheld may comport with due process where "a particularly egregious act has resulted in only a small amount of economic damages." The converse is also true, however. When compensatory damages are substantial, then a lesser ratio, perhaps only equal to compensatory damages, can reach the outermost limit of the due process guarantee. The precise award in any case, of course, must be based upon the facts and circumstances of the defendant's conduct and the harm to the plaintiff.

State Farm Mut. Auto. Ins. v. Campbell, 538 U.S. 408, 425 (2003) (citing BMW of N. Am., Inc. v. Gore, 517 U.S. 559, 582 (1996) ("[P]ositing that a higher ratio might be necessary where 'the injury is hard to detect or the monetary value of noneconomic harm might have been difficult to determine'" (quoting BMW of N. Am, Inc. v. Gore, 517 U.S. 559, 582 (1996)))). *See also* Rendleman, *supra* note 75, at 998 n.100 (suggesting the new maximum for punitive damages may be the amount of compensatory damages (citing Exxon Shipping Co. v. Baker, 554 U.S. 471, 514 (2008))).

290. Enstar Grp., Inc. v. Grassgreen, 812 F. Supp. 1562, 1582 (M.D. Ala. 1993) (examining the ratio of punitive damages to compensatory damages under various assumptions, none of which included compensation forfeiture as either compensatory or punitive damages).

700%.[291] In Texas, the plaintiff must prove at least some actual damages to warrant punitive damages, but it has been held that the dollar value of remedies in equity can be used as a proxy for actual damages.[292] Thus, at least in Texas, the award of forfeiture or disgorgement of compensation might actually justify the award of more punitive damages than without the forfeiture remedy.[293] The only restraint on excessive deterrence remedies is the equitable discretion of the trial judge,[294] which includes the right to deny disgorgement when it appears inequitable.[295]

By itself, compensation forfeiture is the simplest form of disgorgement

291. *See infra* App. 1.

292. *See* Int'l Bankers Life Ins. v. Holloway 368 S.W.2d 567 (Tex. 1963) (indicating "recovery of the consideration paid as a result of fraud," which is a remedy in equity in nature, "constitutes actual damages, and will serve as a basis for the recovery of exemplary damages"); Russell v. Truitt, 554 S.W.2d 948, 955 (Tex. Civ. App.—Fort Worth 1977, writ ref'd n.r.e.) ("The forfeiture of the $8,000 in agency fees is a form of equitable relief awarded for the breach of the equitable duties of those in a fiduciary role. Accordingly, no actual damages are necessary to support the exemplary damage award." (citation omitted)). *But see* Nabours v. Longview Sav. & Loan Ass'n, 700 S.W.2d 901, 904 (Tex. 1985) (denying punitive damages because there was "no finding of actual damage by the jury"). In *Nabours*, although the result seems contrary to the position that punitive damages attach to equitable remedies, the court clearly indicates they were constrained by the jury's limited consideration of actual damages. *Id.* at 905 ("Our holding . . . should not be confused with an absolute refusal to allow punitive damages in a case where equitable relief is had. . . . 'Texas courts . . . will not deny exemplary damages simply because an action is equitable, rather than legal.' . . . Perhaps if the [plaintiffs] had not so limited the jury's consideration of . . . damages, an adequate damage finding would have been made." (quoting Mack v. Newton, 737 F.2d 1334, 1363 (5th Cir. 1984))).

293. In *Consolidated Texas Financial v. Shearer*, the court demonstrates punitive damages can be conditioned on remedies in equity as well as on actual damages. *See* Consol. Tex. Fin. v. Shearer, 739 S.W.2d 477, 480 (Tex. App.—Fort Worth 1987, no writ) (recognizing Texas "require[es] actual damages as a prerequisite for exemplary damages" but stating the reasoning behind that requirement would also allow punitive damages to attach to a relief in equity). Here, the plaintiffs had the choice between taking equitable relief or receiving actual damages; it chose the former but still asked for punitive damages. *Id.* at 479. The defendant argued no punitive damages could attach since no actual damages were awarded to the plaintiff, but the court disagreed. *See id.* at 480 (stressing, while "no actual damages were awarded"—because the remedy in equity was elected by the plaintiffs—the jury still found actual damages existed; thus, the court was able to "concentrate on the conduct of the wrongdoer" and award punitive damages on top of the equitable relief).

294. *See Grassgreen*, 812 F. Supp. at 1574, 1575 (acknowledging, while some equitable remedies may be more or less favored in certain situations, the court retains the flexibility to exercise its judicial discretion on whether to impose those remedies as a deterrence to future wrongdoers; the court notes: it is "of crucial importance to the economic well-being of this country for corporate officers and directors to understand without question that in the discharge of the duties of their offices[,] they must subordinate their personal interests to the interests of the corporation which they serve").

295. *See* Nat'l R.R. Passenger Corp. v. Veolia Transp. Servs., Inc., 886 F. Supp. 2d 14, 19–20 (D.D.C. 2012) ("When 'liability for the profits so designated would be unacceptably punitive, being unnecessary to accomplish the object of the disgorgement remedy in restitution,' courts may deny disgorgement, even if some level of attribution exists." (quoting RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 51 cmt. f (AM. LAW INST. 2011))).

as the measure of unjust enrichment generally denies the defendant credit for his compensation.[296] Even so, some trial judges perceive compensation forfeiture as excessive in general or as excessive in that case.[297] *Astra USA, Inc., v. Bildman*[298] is a typical example; if the trial judge had been allowed to exercise her unfettered discretion, she would not have awarded any forfeiture or punitive damages even though the egregiousness factor would seem high.[299]

Appendix 1 of this Article compares the remedy packages of four of the cases discussed in Section II and six others (as well as one case of asset forfeiture). It shows that compensation forfeiture can exceed the amount of compensatory and consequential damages and that the ratio of the sum of compensation forfeiture and punitive damages to all other remedies ranged from 2% to 940% with a simple average of 430% for the ten cases.[300]

Separately, the remedies of disgorgement and punitive damages are justified as necessary to deter a fiduciary's temptation to breach her trust. In modern times, most courts permit awarding punitive damages for

296. *See* Crites, Inc. v. Prudential Ins. Co., 322 U.S. 408, 416–18 (1944) (affirming the disgorgement of 100% of the secret profits from the lawyer fiduciaries and the denial of payment for any additional compensation); Hahn v. OnBoard, LLC, No. 09-3639, 2011 WL 703836, at *6 (D.N.J. Feb. 18, 2011) ("When an employee violates the duty of loyalty, the employer 'has a choice of remedies' to recover any benefits conferred upon the employee during the period of disloyalty, including wages paid to the employee." (quoting W. Elec. Co. v. Brenner, 360 N.E.2d 1091, 1094 (N.Y. 1977))); Henderson v. Rep Tech, Inc., 557 N.Y.S.2d 224, 225 (App. Div. 1990) ("The compensation paid an employee during the period of disloyalty is a component of the profit for which an employee must account and is subject to forfeiture." (citation omitted)); Int'l Bankers Life Ins. Co. v. Holloway, 368 S.W.2d 567, 577 (Tex. 1963) (affirming disgorgement of 100% of the directors' secret profits and the denial of any offsetting compensation); *see also* RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 43 cmt. d, illus. 10–12 & cmt. h (AM. LAW INST. 2011) (portraying the remedies of forfeiture and restitution upon breach of fiduciary duty).

297. *See* Bank of Tokyo–Mitsubishi, Ltd. v. Malhotra, 131 F. Supp. 2d 959, 962 (N.D. Ill. 2000) (calling total forfeiture of compensation for nine years "extraordinarily punitive" and uncalled for); *see also* Price Waicukauski & Riley, LLC v. Murray, 47 F. Supp. 3d 810, 827 (S.D. Ind. 2014) ("Professor Tidmarsh opined that PWR should have obtained written consent for the dual representation of the Murrays and the plaintiffs in the Russell action. While the Court agrees that this may have been the most prudent course of action, in all, the Court does not see any equity in disgorging PWR of $2.7 million in attorney fees for failing to do so." (citation omitted)).

298. Astra USA, Inc. v. Bildman (*Bildman III*), Nos. 980580C, 991942G, 2006 WL 760283 (Mass. Dist. Ct., Super. Ct. Jan. 26, 2006).

299. *See id.* at *20–21 ("Here, Bildman's breach of fiduciary duty constitutes serious misconduct. In weighing the equities, however, this court considers that some of Bildman's unsavory behavior may have been in keeping with Astra's corporate culture at the time in question, and tolerated, at least for a time, by the directors."), *aff'd in part*, *rev'd in part*, 914 N.E.2d 36 (Mass. 2009); *see also* Sealed Party v. Sealed Party, No. Civ.A. H-04-2229, 2006 WL 1207732, at *21 (S.D. Tex. May 4, 2006) (denying forfeiture even though a breach of fiduciary duty was found).

300. *See infra* App. 1.

claims of breach of fiduciary duty and, occasionally, will even stack punitive damages on top of disgorgement or forfeiture.[301] When all three remedies are combined, the court is awarding three remedies to deter future breaches; yet, there is no generally acknowledged practice to adjust for the award of the other remedies.[302] Seemingly, the rationale of deterrence is not a blank check for an excessive combination of remedies; i.e., after a point, it is unreasonable to expect a greater amount of remedies to meaningfully add to the deterrence.[303]

Furthermore, some states distinguish between punishment and destruction as legitimate goals for punitive damages. In *Enstar Group, Inc. v. Grassgreen*,[304] for example, the trial judge noted Alabama law intends exemplary damages to punish but not destroy the defendant.[305] Yet, it seems clear that the policy behind a legal process that allows compensation forfeiture and punitive damages to be stacked at least tolerates the financial ruin of the defendant to result.[306] How many people today, even among the highest paid, have sufficient reserves to undergo expensive litigation,

301. *See In re* Marriage of Pagano, 607 N.E.2d 1242, 1249–50 (Ill. 1992) (noting forfeiture may be justified as matter of public policy when the breach is "egregious" and stating "punitive damages are *permissible* where a duty based on a relationship of trust is violated, the fraud is gross, or malice or willfulness are shown"). For a summary of cases that have stacked multiple remedies, see *infra* App. 1.

302. Rendleman, *supra* note 75, at 980 ("The principal distinction between compensatory damages and restitution is that compensatory damages respond to the plaintiff's loss, restitution to the defendant's gain. Although both deter, if restitution exceeds compensatory damages, restitution will deter more. . . . The court imposes punitive damages on a defendant to punish it and to deter it and others from misconduct." (footnote omitted)).

303. *Id.* at 1002 ("We turn from choosing either restitution or punitive damages to adding punitive damages to restitution, restitution plus punitive damages. We bridge a watershed to cross from restitution to prevent defendant's unjust enrichment with its policy base of deterring misconduct to punitive damages with the policy base of deterrence plus punishment.").

304. Enstar Grp., Inc. v. Grassgreen, 812 F. Supp. 1562 (M.D. Ala. 1993).

305. *Id.* at 1580 ("[O]nly in the rarest of cases should [the damages] be large enough to destroy [the defendant]."); *see also* Maxwell v. Aetna Life Ins., 693 P.2d 348, 362 (Ariz. Ct. App. 1984) ("While the verdict must be sufficient to punish and deter others in similar circumstances, it must not financially kill the defendant." (citation omitted)); Ace Truck & Equip. Rentals v. Kahn, 746 P.2d 132, 135 (Nev. 1987) ("The most frequently cited rule is that the amount of punitive damages assessed should be sufficient to punish a wrongdoer and deter others from acting in a similar manner without financially annihilating the defendant."), *abrogated by* Bongiori v. Sullivan, 138 P.3d 433 (Nev. 2006).

306. *See Bildman II*, Nos. 980580C, 991942G, 2006 WL 760283, at *8 (Mass. Dist. Ct., Super. Ct. Jan. 26, 2006) (suggesting a defendant could suffer substantial financial ruin and "forfeit his entire compensation" as a result of his breach of fiduciary duty if he fails to meet his burden of proof), *aff'd in part*, *rev'd in part*, 914 N.E.2d 36 (Mass. 2009); *see also* Bank of Tokyo–Mitsubishi, Ltd. v. Malhotra, 131 F. Supp. 2d 959, 962 (N.D. Ill. 2000) (disapproving of the harsh result to a defendant by calling total forfeiture of compensation "extraordinarily punitive" and uncalled for).

to pay substantial compensatory or consequential damages as well as punitive damages, and then also to pay back to the employer three to five years of gross compensation? It seems very unlikely that Aramony, Bildman, or Gittlitz survived the payment of their judgments without financial ruin.

B. *Categories of Remedies Available for Breach of Fiduciary Duty*

Compensatory damages include out-of-pocket or incidental losses such as wasted assets,[307] travel and entertainment expense fraud,[308] the cost to replace lost assets such as retraining personnel,[309] and lost profits.[310]

A claim for lost profits is mutually exclusive with disgorgement,[311] which is pled in the alternative[312] and is awarded as a proxy for the

307. *See Bildman II*, 2006 WL 760283, at *1 (awarding plaintiff $1,040,812 in damages after finding defendant liable for wasting plaintiff's assets, breach of fiduciary duty, failure to disclose material information, and improper use of plaintiff's funds).

308. *See, e.g.*, ICD Publ'ns, Inc. v. Gittlitz, 2014 IL App (1st) 133277, ¶ 34 (awarding damages for accumulated fraudulent transactions over seven years for $1,220,623).

309. *See* Chelsea Indus., Inc. v. Gaffney, 449 N.E.2d 320, 330 n.23 (Mass. 1983) (explaining the principal was entitled to the cost of training the replacement of two employees that the defendant had tortuously interfered with (citing Frederick Chusid & Co. v. Marshall Leeman & Co., 326 F. Supp. 1043, 1060–61 (S.D.N.Y. 1971))).

310. *See* Dowd & Dowd, Ltd. v. Gleason, 816 N.E.2d 754, 770–71 (Ill. App. Ct. 2004) (awarding $871,199 in lost profits in addition to other compensatory damages); *see also* Vigneau v. Storch Eng'rs, No. CV 890700122S, 1995 WL 767984, at *8 (Conn. Super. Ct. Dec. 4, 1995) (awarding compensatory damages of $58,923 for lost profits in a claim for disloyal competition); Swinnea v. ERI Consulting Eng'rs, Inc. (*Swinnea III*), 364 S.W.3d 421, 424–25 (Tex. App.—Tyler 2012, pet. denied) (reducing lost profits from $300,000 to $178,601, affirming the punitive damages of $1 million and remanding the asset forfeiture to the trial court for consideration of the factors enumerated in the Supreme Court opinion).

311. *See* Vibra–Tech Eng'rs, Inc. v. Kavalek, 849 F. Supp. 2d 462, 488–89, 501 (D.N.J. 2012) (awarding the higher of lost profits or disgorgement). *But see* Saden v. Smith, 415 S.W.3d 450, 470–72 (holding it was incorrect to award damages for both breach of contract and breach of fiduciary duty, instead awarding lost profits just for the breach of contract, but in a mistaken juxtaposition of profit disgorgement for compensation forfeiture, also awarding the same in disgorgement of profits). This particular issue is further explored in Section V.B. *See also* Rendleman, *supra* note 75, at 981 (stating compensatory damages and restitution are mutually exclusive and frequently left to the choice of the plaintiff).

312. *See* McGowan & Co. v. Bogan (*Bogan II*), No. H-12-1716, 2015 WL 3422366, at *6 (S.D. Tex. May 27, 2015) ("Plaintiff clarifies that it seeks 'lost profits' or, in the alternative, 'the amount Bogan was unjustly enriched.'"); *In re* Longview Energy Co., 464 S.W.3d 353, 361 (Tex. 2015) ("Disgorgement is compensatory in the same sense attorney fees, interest, and costs are, but it is not damages. Indeed, Longview has itself made clear that it sought disgorgement instead of damages, and did not request jury findings on damages, because it thought the Eagle Ford shale assets were undervalued."); *see also* Saint Alphonsus Diversified Care, Inc. v. MRI Assocs., 334 P.3d 780, 801 (Idaho 2014) ("The loss of value award to MRI Center of $25,420,000 was an alternative to its award of lost profits in the sum of $25,828,208, and the disgorgement award of $21,353,838 was in alternative to all other awards to the MRI Entities, the largest of which total $52,084,513."); Quality

plaintiff's damages in other areas of the law.[313] Further, a claim for lost future profits is mutually exclusive with future disgorgement[314] and

Health Care Mgt. Inc. v. Kobakhidze, No. 27234/10, slip. op. at 7 (N.Y. Sup. Ct. Feb. 22, 2013) ("[T]he purpose of damages for such breach was not only to compensate for wrongs, but to prevent them[;] . . . a prevailing plaintiff may elect the remedy for such a breach to be calculated as either the disgorgement of the gain . . . or the employer's lost profits." (first citing Diamond v. Oreamuno, 248 N.E.2d 910, 912 (N.Y. 1969); and then citing Gomez v. Bicknell, 756 N.Y.S.2d 209, 214 (App. Div. 2002))).

313. Disgorgement has been used as a proxy for the plaintiff's damages in claims relating to breach of fiduciary duty. *See* Meister v. Mensinger, 178 Cal. Rptr. 3d 604, 618 (Ct. App. 2014) ("Typically, the defendant's benefit and the plaintiff's loss are the same, and restitution requires the defendant to restore the plaintiff to his or her original position." (quoting Cty. of San Bernardino v. Walsh, 69 Cal. Rptr. 3d 848, 855 (Ct. App. 2008))); Arabesque Studios, Inc. v. Acad. of Fine Arts, Int'l, Inc., 529 S.W.2d 564, 569 (Tex. Civ. App.—Dallas 1975, no writ) (holding the new employer's profits could be used to measure damages for a prior employer's damages in the case of an employee's breach of covenant to not compete). Disgorgement has also been used as a damages proxy for claims relating to misappropriation of intellectual property. *See* Swofford v. B & W, Inc., 336 F.2d 406, 411 (5th Cir. 1964) ("The profits which were recoverable in equity against an infringer of a patent were compensation for the injury the patentee had sustained from the invasion of his rights. Such profits were considered the measure of the patentee's damages. It was very early recognized that, 'though called profits, they are really damages.'" (quoting Mowry v. Whitney, 81 U.S. (14 Wall.) 620, 653 (1872))); Sandare Chem. Co. v. WAKO Int'l, Inc., 820 S.W.2d 21, 23 (Tex. App.—Fort Worth 1991, no writ) ("An unjust enrichment measure of damages is appropriate for wil[l]ful interference with contractual relations, at least where the plaintiff's lost profits are not readily ascertainable."); Att'y Gen. v. Blake, [2000] 1 AC 268, 279–80 (HL) ("Thus, in 1803 Lord Eldon L.C. stated, in *Hogg v. Kirby* a passing off case: 'what is the consequence in Law and in Equity? . . . [A] Court of Equity in these cases is not content with an action for damages; for it is nearly impossible to know the extent of the damage; and therefore the remedy here, though not compensating the pecuniary damage except by an account of profits, is the best: the remedy by an injunction and account.'" (citation omitted)); RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 42 cmt. d (AM. LAW INST. 2011) ("To the extent that the defendant's profits from infringement represent profits the plaintiff would otherwise have earned, the calculation of 'infringer's profits' becomes an indirect mode of showing 'plaintiff's damages,' and the same amount might be recovered under either heading."); 1 GEORGE E. PALMER, THE LAW OF RESTITUTION § 2.7, at 87–88 (1978) ("[I]n a suit in equity for infringement of patent or copyright, the patent or copyright holder was entitled to recover the profits made through the infringement. Although . . . sometimes explained . . . [as a measure of damages], it was clear that the relief was based on unjust enrichment . . . ." (footnotes omitted)).

314. For cases discussing future unjust enrichment, see *Children's Broadcasting Corp. v. Walt Disney Co.*, 357 F.3d 860, 869 (8th Cir. 2004) (finding prejudgment interest applies only to current damages not future damages), *Broan Manufacturing Co. v. Associated Distributors, Inc.*, 923 F.2d 1232, 1237 (6th Cir. 1991) (holding the jury's calculation of future damages was not "speculative"), *Financial Programs, Inc. v. Falcon Financial Services Inc.*, 371 F. Supp. 770, 778–79 (D. Or. 1974) (holding, under Oregon law, damages for future loss of profits must be based on something more than mere speculation and guesswork), *American Speedy Printing Centers, Inc. v. AM Marketing, Inc.*, 69 F. App'x 692, 699 (6th Cir. 2003) (awarding franchisor "lost future profits" after finding it was based on a reasonable degree of certainty), *JTH Tax Inc. v. H & R Block Eastern Tax Services*, 245 F. Supp. 2d 749, 750–51 (E.D. Va. 2002) (calculating six years of future earnings in terms of their net present value), *Whiteside Biomechanics v. Sofamor Danek Group*, 88 F. Supp. 2d 1009, 1020 (E.D. Mo. 2000) (recognizing the jury's verdict at the trial level incorporated future damages), and *Dozor Agency, Inc. v. Rosenberg*,

injunctive relief.[315] Thus, the claimant for disloyal competition can either claim lost future unjust enrichment or lost future profits, or seek to enjoin the defendant's competition but not both.[316] A third alternative to lost profits or disgorgement is the claimant's lost enterprise value.[317]

Like future lost profits or future unjust enrichment, an award of consequential damages as a remedy in equity for a breach of fiduciary duty is also possible, but it requires strong justification.[318] As a remedy at law, it would require the standard proof of causation; although, the plaintiff should expect additional scrutiny as the damages alleged appear more and more remote.[319]

218 A.2d 583, 586 (Pa. 1966) (using the present value of projected income to calculate damages).

315. *See* Next Level Commc'ns LP v. DSC Commc'ns Corp., 179 F.3d 244, 254 (5th Cir. 1999) (rejecting appellee's argument that "it was entitled to a limited permanent injunction in addition to monetary damages to prevent the transfer or disclosure of its trade secrets"); AngioScore, Inc. v. TriReme Med., Inc., No. 12-CV-03393-YGR, 2015 WL 4040388, at *32 (N.D. Cal. July 1, 2015) (awarding the plaintiff "[1] its current lost profits of $2.97 million, representing the profits it would have generated had business not been diverted to defendants, and [2] its future lost profits"); Home Pride Foods, Inc. v. Johnson, 634 N.W.2d 774, 784 (Neb. 2001) ("The court's award for the value of future sales is inconsistent with the issuance of a permanent injunction.").

316. *See Next Level Commc'ns*, 179 F.3d at 254 (affirming the district court's refusal to grant an injunction since the claimant had already been made whole by the monetary damages awarded).

317. *See* Prime Mortg. USA, Inc. v. Nichols, 885 N.E.2d 628, 638, 654 (Ind. Ct. App. 2008) (reversing on other grounds but affirming the trial court's judgment, "awarding Nichols $2,500,000 in compensatory damages for the value of her 50% ownership in Prime, trebled to $7,500,000; $6,330.02 in unpaid wages, trebled to $18,990.06; and $402,891.28 in attorney's fees."); *see also* Vendo Co. v. Stover, 321 N.E.2d 1, 3, 13–15 (Ill. 1974) (affirming an award of $7,345,000, which included $2,135,000 of lost profits, $170,835 of compensation forfeiture—against the president of the defendant–corporation—and $5,039,165 of lost value of the employer's enterprise).

318. *See* Milbank, Tweed, Hadley & McCloy v. Boon, 13 F.3d 537, 543 (2d Cir. 1994) (affirming the award of consequential damages, believing the breach was serious enough to justify applying a "prophylactic rule," which lessens the burden for showing cause). According to the Restatement (Third) of Restitution & Unjust Enrichment:

> Disgorgement liability by the rule of § 43 is not restricted to conscious wrongdoers. In contrast to the property-based rules of §§ 40[–]42, the prophylactic aims of fiduciary duty require a fiduciary to disgorge profits (including consequential gains) even if the breach of duty is inadvertent. The same liability is imposed on a third party who acquires a benefit with notice of the fiduciary's breach of duty. By contrast, an innocent third party who obtains property as a result of another's breach of trust is liable to make restitution of what has been received but not for consequential gains.

RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 43 cmt. h (AM. LAW INST. 2011) (citations omitted).

319. In Texas, the standard is proximate cause. *See* Yaquinto v. Segerstrom (*In re* Segerstrom), 247 F.3d 218, 225–26 (5th Cir. 2001) (concluding injury and causation were not adequately shown to support a judgment awarding damages for breach of fiduciary duty). In New York, the standard is either proximate cause or substantial factor. *But see Aramony III*, 191 F.3d 140, 154 n.7 (2d Cir. 1999) (noting the substantial factor test may be inappropriate when compensatory damages are sought over restitution).

Compensation forfeiture requires no proof of other damages[320] and is not mutually exclusive with other remedies.[321] Alternatively, the claimant can accomplish implicit forfeiture by ensuring the exclusion of any credit or offset for the fiduciary's compensation in either an accounting in equity or in the measure of the defendant's unjust enrichment.[322]

Punitive damages are also available in most states with the noted exception of Delaware.[323] However, in determining whether a claim is in equity or at law, a plea for punitive damages is generally still regarded as a remedy at law.[324]

Remedies in equity are also available in addition to the categories above

320. *See* Woods v. City Nat'l Bank & Tr. Co. of Chi., 312 U.S. 262, 268 (1941) ("Where an actual conflict of interest exists, no more need be shown in this type of case to support a denial of compensation.").

321. RESTATEMENT (THIRD) OF AGENCY § 8.01 cmt. d (AM. LAW INST. 2006) ("Forfeiture may be the only available remedy when it is difficult to prove that harm to a principal resulted from the agent's breach or when the agent realizes no profit through the breach. In many cases, forfeiture enables a remedy to be determined at a much lower cost to litigants.").

322. *See* Hahn v. OnBoard, LLC, No. 09-3639, 2011 WL 703836, at *6 (D.N.J. Feb. 18, 2011) ("When an employee violates the duty of loyalty, the employer 'has a choice of remedies' to recover any benefits conferred upon the employee during the period of disloyalty, including wages paid to the employee." (quoting W. Elec. Co. v. Brenner, 360 N.E.2d 1091, 1094 (N.Y. 1977))); Henderson v. Rep Tech, Inc., 557 N.Y.S.2d 224, 225 (App. Div. 1990) ("The compensation paid an employee during the period of disloyalty is a component of the profit for which an employee must account and is subject to forfeiture." (citation omitted)); *see also* RESTITUTION & UNJUST ENRICHMENT § 43 cmt. d, illus. 10–12 & cmt. h (portraying the remedies of forfeiture and restitution upon breach of fiduciary duty).

323. *See* AGENCY § 8.01 cmt. d. ("A breach of fiduciary duty may also subject the agent to liability for punitive damages when the circumstances satisfy generally applicable standards for their imposition."). For examples of punitive damages, see *infra* App. 1. For a Delaware case that denies punitive damages as a matter of law, see *Albert v. Alex. Brown Management Services, Inc.*, Nos. C.A. 04C-05-250 PLA, C.A. 04C-05-251 PLA, 2004 WL 2050527, at *6 (Del. Super. Ct. Sept. 15, 2004) ("While it is true that a fraud allegation can support punitive damages, many types of fraud, including all those involving breach of fiduciary duty, are heard exclusively in Chancery without possibility of punitive damages.").

324. *Sommers Drug Stores Co. Employee Profit Sharing Trust v. Corrigan Enterprises., Inc.* illustrates the distinction:

> "Equitable or remedial" relief generally includes all of the kinds of relief available to restore the plaintiff's losses or protect him from future harm . . . . Punitive damages do not fall within the broad category of "equitable or remedial" relief; rather than restoring the plaintiff's losses and protecting him from future harm, punitive damages are designed to punish the wrongdoer and deter others from similar misconduct.

Summers Drug Stores Co. Emp. Profit Sharing Tr. V. Corrigan Enters., Inc., 793 F.2d 1456, 1463 (5th Cir. 1986); *see also* Prime Mortg. USA, Inc. v. Nichols, 885 N.E.2d 628, 643–44 (Ind. Ct. App. 2008) (concluding one of the plaintiff's claims sounded in equity and the others in law, since the "claim for breach of fiduciary duty is an equitable claim" but "actions for money damages are considered legal in nature").

or instead of compensatory or consequential damages. As both the Restatement (Second) of Agency and Professor Laycock point out, a remedy in equity is especially important when it is the only remedy available.[325] A number of cases have approved a remedy in equity where damages were difficult or too speculative to award.[326]

If the disloyal fiduciary transfers legal title to an asset that needs to be changed or executes a contract that needs to be amended or voided, injunctive relief or in personam authority will be required.[327] An accounting in equity or a constructive trust may be needed to allow the court to supervise further discovery[328] or grant the principal a security

325. *See* RESTATEMENT (SECOND) OF AGENCY § 399 cmt. e (AM. LAW INST. 1958) (recognizing "equitable relief may be granted . . . when there is no adequate remedy at law, as where an injunction is granted"). Professor Laycock Points to three circumstances where restitutionary claims matter:

> (1) when unjust enrichment is the only source of liability; (2) when plaintiff prefers to measure recovery by defendant's gain, either because it exceeds plaintiff's loss or because it is easier to measure; and (3) when plaintiff prefers specific restitution, either because defendant is insolvent, because the thing plaintiff lost has changed in value, or because plaintiff values the thing he lost for nonmarket reasons.

Laycock, *supra* note 8, at 1284; *cf.* Next Level Commc'ns LP v. DSC Commc'ns Corp., 179 F.3d 244, 254 (5th Cir. 1999) (denying equitable relief since the plaintiff was "made whole by the damages award" and thus was not entitled to any additional relief).

326. In *Woods v. City National Bank*, the Court notes, "[T]he incidence of a particular conflict of interest can seldom be measured with any degree of certainty." Woods v. City Nat'l Bank & Tr. Co. of Chi., 312 U.S. 262, 268 (1941). But, instead of speculating how the conflict arose or the true intentions behind it, the Court reasons, "Where an actual conflict of interest exists, no more need be shown . . . to support a denial of compensation." *Id.*; *see also* Nichols v. Minnick, 885 N.E.2d 1, 5 (Ind. 2008) (explaining one reason harm to the plaintiff may not be required is that "disgorgement may be 'the only available remedy' for an agent's breach of fiduciary duty because harm to the principal is difficult to prove" (quoting RESTATEMENT (THIRD) OF AGENCY § 8.01 cmt. d (AM. LAW INST. 2006))); Maritrans GP Inc. v. Pepper, Hamilton & Scheetz, 602 A.2d 1277, 1287 (Pa. 1992) (asserting the former client–appellant's "remedy at law . . . would be difficult if not impossible to sustain because of difficult problems of proof, particularly problems related to piercing what would later become a confidential relationship between their competitors and those competitors' attorneys"); United Bd. & Carton Corp. v. Britting, 164 A.2d 824, 833 (N.J. Super. Ct. Ch. Div. 1959) ("It is a well established rule that equity will intervene to grant equitable relief when the damages at law are inadequate, or not readily calculable."), *aff'd and modified per curiam*, 160 A.2d 660 (N.J. Super. Ct. App. Div. 1960).

327. 1 DOBBS, *supra* note 6, § 4.4, at 625 ("If the plaintiff traces his real property into the hands of the defendant and the plaintiff is entitled to restitution, then specific restitution is appropriate. If a court wants to speak of rescission rather than constructive trust, an order requiring specific restitution is still appropriate.").

328. *See* Mar. Fish Prods., Inc. v. World-Wide Fish Prods., Inc., 474 N.Y.S.2d 281, 287 (App. Div. 1984) ("Thus, an accounting is warranted to ascertain the damages resulting from [the employee's] diversion of business during the entire fourteen-month period from December 1975, when he incorporated World-Wide, until February 11, 1977, when he resigned from Maritime."); *see also* Durwood v. Dubinsky, 361 S.W.2d 779, 790 (Mo. 1962) (reasoning an employer "usually has an

position against the defendant.[329]

When the principal sues a third party, such as a competitor, it can claim either damages or unjust enrichment against the third party and still sue the fiduciary for any profit or benefit that he retained, as well as his compensation.[330] In some circumstances, the principal can also collect legal costs from the fiduciary for the expense of having to sue the third party.[331]

C. *Causation and Burden of Proof*

There is a substantial difference between the evidence required for a prima facie case for breach of fiduciary duty in a claim based on a remedy in equity and a claim based on a remedy at law.[332] Thus, a claim for

action at law for damages" for an employee's "improper conduct"; however, when the actual damages "would be speculative and not subject to proof[,] . . . . a court of equity will, in the proper circumstances, afford relief to the employer by the imposition of a constructive trust in his favor on the profits and property wrongfully acquired by the employee").

329. *See* Radenhausen v. Doss, 819 So. 2d 616, 620 (Ala. 2001) ("A constructive trust may be impressed upon property when the grantee of the property has abused a confidential relationship with the grantor." (quoting Jordan v. Mitchell, 705 So. 2d 453, 461 (Ala. Civ. App. 1997))); Schock v. Nash, 732 A.2d 217, 231 (Del. 1999) (affirming the trial court's imposition of a constructive trust against the fiduciary in breach and members of her family to secure assets wrongfully removed from a trust account); Lerner Corp. v. Three Winthrop Props., Inc., 723 A.2d 560, 566 (Md. Ct. Spec. App. 1999) ("Where a fiduciary[,] in violation of his duty to the beneficiary[,] acquires property through the use of confidential information, he holds the property so acquired upon a constructive trust for the beneficiary." (quoting RESTATEMENT (FIRST) OF RESTITUTION & UNJUST ENRICHMENT § 200 (AM. LAW INST. 1937))).

330. In *Tarnowski v. Resop*, the court explains the principal's right to recover the profits made by the employee is not affected by his separate recovery of damages:

> If an agent has violated a duty of loyalty to the principal so that the principal is entitled to profits which the agent has thereby made, the fact that the principal has brought an action against a third person and has been made whole by such action does not prevent the principal from recovering from the agent the profits which the agent has made.

Tarnowski v. Resop, 51 N.W.2d 801, 803 (Minn. 1952) (quoting RESTATEMENT (SECOND) OF AGENCY § 407 cmt. e (AM. LAW INST. 1958)); *see also* RESTATEMENT (THIRD) OF AGENCY § 8.01 cmt. b (AM. LAW INST. 2006) ("A third party who, knowing that the agent's conduct constitutes a breach of duty, provides substantial assistance to the agent is also subject to liability to the principal.").

331. *See Tarnowski*, 51 N.W.2d at 804 (recognizing the "attorneys' fees and expenses of suit were directly traceable to the harm caused by defendant's wrongful act[;] [a]s such, they are recoverable" (citation omitted)); 22 AM. JUR. 2D *Damages* § 450 (2013) ("If, through the wrongful act of the present adversary, a party is involved in earlier litigation with a third person in bringing or defending an action to protect the first party's interests, that party is entitled to recover the reasonable value of attorney's fees . . . incurred because of that litigation.").

332. In *Yaquinto v. Segerstrom*, the court acknowledges this difference:

> While the Texas Supreme Court has dispensed with the need to prove an actual injury and

compensation forfeiture has a lesser burden of proof because compensation forfeiture is treated as a remedy in equity for which proof of loss is not required.[333] Note the passive language in the Restatement (Third) of Restitution and Unjust Enrichment that is used to avoid a requirement for causation or scienter for remedies in equity.[334] The Restatement also specifically disclaims proof of a benefit to the fiduciary, which is contrary to what some states' laws hold, including Texas.[335]

causation when a plaintiff seeks to forfeit some portion of an attorney's fees in connection with a breach of fiduciary duty, injury and causation are still required when a plaintiff seeks to recover damages for a breach of fiduciary duty.

Yaquinto v. Segerstrom (*In re* Segerstrom), 247 F.3d 218, 225 n.5 (5th Cir. 2001) (citation omitted); *see* Hendry v. Pelland, 73 F.3d 397, 401 (D.C. Cir. 1996) (acknowledging some jurisdictions require "clients . . . prove injury and proximate causation in a fiduciary duty claim against their lawyer if they seek *compensatory damages*, not if . . . they seek only *forfeiture of legal fees*"); Arst v. Stifel, Nicolaus & Co., 954 F. Supp. 1483, 1488–89 (D. Kan. 1997) (holding where the plaintiff merely sought disgorgement of profits and was not seeking damages, he was not "required to show materiality and causation of the non-disclosure"); *see also* Deborah A. DeMott, *Causation in the Fiduciary Realm*, 91 B.U. L. REV. 851, 867–68 (2011) [hereinafter DeMott, *Causation in the Fiduciary Realm*] (stating "the causal standard seems a function of the remedy sought by the beneficiary, because restitutionary remedies—including forfeiture of fees otherwise due a disloyal lawyer—escape the stringency of 'but-for' causation").

333. *See* Woods v. City Nat'l Bank & Tr. Co. of Chi., 312 U.S. 262, 268 (1941) (stating as long as "an actual conflict of interest exists, no more need be shown . . . to support a denial of compensation"); Magruder v. Drury, 235 U.S. 106, 120 (1914) ("While no wrong was intended, and none was in fact done to the estate, we think nevertheless that upon the principles governing the duty of a trustee, the contention that this profit could not be taken by [the trustee], owing to his relation to the estate, should have been sustained."); United States v. Carter, 217 U.S. 286, 306 (1910) ("It would be a dangerous precedent to lay down as law that unless some affirmative fraud or loss can be shown, the agent may hold on to any secret benefit he may be able to make out of his agency."); People *ex rel.* Plugger v. Twp. Bd. of Overyssel, 11 Mich. 222, 225–26 (1863) (clarifying "[f]idelity in the agent" not "[a]ctual injury" is the law's primary purpose behind voiding transactions, noting "the law will not permit the agent to place himself in a situation in which he may be tempted by his own private interest to disregard that of his principal").

334. RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 43 cmt. a (AM. LAW INST. 2011) ("If restitution takes the form of a liability to disgorge profits, a disloyal fiduciary—without regard to notice or fault—is treated as a conscious wrongdoer (§ 51(3)); though a defendant who obtains a benefit in consequence of another's breach of fiduciary duty, within the rule of § 43(c), might be treated for restitution purposes as an innocent recipient (§ 50)."); *see also* DeMott, *Causation in the Fiduciary Realm*, *supra* note 332, at 853 ("Each side of fiduciary liability also uses a distinctive vocabulary. Within restitution, a disloyal fiduciary 'obtains' or 'derives' benefits through wrongful conduct, terms that hint at causal connections but do not explicitly articulate them." (footnote omitted)).

335. RESTITUTION & UNJUST ENRICHMENT § 43 cmt. b (dispensing the need to show "the claimant has sustained quantifiable economic injury or that the defendant has earned a net profit from the transaction"); *see also* Foley v. Am. Elec. Power, 425 F. Supp. 2d 863, 874 (S.D. Ohio 2006) ("There is no requirement that an agent receive a benefit before the faithless servant doctrine authorizes a forfeiture of the agent's compensation."); ERI Consulting Eng'rs, Inc. v. Swinnea (*Swinnea II*), 318 S.W.3d 867, 873 (Tex. 2010) ("[E]ven if a fiduciary does not obtain a benefit from a third party by violating his duty, a fiduciary may be required to forfeit the right to compensation for

The elements of a prima facie claim in equity for breach of fiduciary duty are less rigorous than a claim at law.[336] For remedies at law, the claimant must satisfy the normal elements of the claim as provided either in contract or tort law, including proximate cause.[337] In New York there have been at least two cases relating to legal malpractice claims that alleged the defendant lawyers were conflicted, but the claims were dismissed because the clients in those cases sought tort damages without proof of loss.[338] If those claims had been pled as claims for compensation forfeiture, they could have avoided those grounds for dismissal.

The goal of remedies in equity is to deny unjust enrichment to the defendant; thus, the principal's damages are irrelevant.[339] For monetary

the fiduciary's work."). But see *Academy of Skills & Knowledge, Inc. v. Charter Schools, USA, Inc.*, noting

> the elements of a breach of fiduciary duty cause of action are (1) a fiduciary relationship must exist between the plaintiff and the defendant, (2) the defendant must have breached its fiduciary duty to the plaintiff, and (3) the defendant's breach must result in injury to the plaintiff or benefit to the defendant.

Acad. of Skills & Knowledge, Inc. v. Charter Schs., USA, Inc., 260 S.W.3d 529, 540 (Tex. App.—Tyler 2008, pet. denied); *see also* Roach, *supra* note 6, at 469–74 (discussing the Texas appellate requirement for proof of defendant–fiduciary's improper benefit for compensation benefit claims against lawyers).

336. *Compare* RESTITUTION & UNJUST ENRICHMENT § 43 ("A person who obtains a benefit (a) in breach of a fiduciary duty, (b) in breach of an equivalent duty imposed by a relation of trust and confidence, or (c) in consequence of another's breach of such a duty, is liable in restitution to the person to whom the duty is owed."), *with* Hunn v. Dan Wilson Homes, Inc., 789 F.3d 573, 581 (5th Cir. 2015) ("The elements of a breach of fiduciary duty claim are: (1) a fiduciary relationship must exist between the plaintiff and defendant; (2) the defendant must have breached his fiduciary duty to the plaintiff; and (3) the defendant's breach must result in injury to the plaintiff or benefit to the defendant." (quoting Graham Mortg. Corp. v. Hall, 307 S.W.3d 472, 479 (Tex. App.—Dallas 2010, no pet.))). Other courts have expressed the elements similarly. *See* Trading LLC v. Wells Fargo Sec., LLC, 553 Fed. App'x 33, 35 (2d Cir. 2014) ("Turning first to Williams's claim for breach of fiduciary duty, the elements of such a claim are: '(i) the existence of a fiduciary duty; (ii) a knowing breach of that duty; and (iii) damages resulting therefrom.'" (quoting Johnson v. Nextel Commc'ns, Inc., 660 F.3d 131, 138 (2d Cir. 2010))); *see also* Ball v. Kotter, 723 F.3d 813, 826 (7th Cir. 2013) ("To succeed in a claim for breach of fiduciary duty, a plaintiff must prove the following elements: (1) a fiduciary duty exists; (2) the fiduciary duty was breached; and (3) the breach proximately caused the injury of which the plaintiff complains." (citing Neade v. Portes, 739 N.E.2d 496, 502 (Ill. 2000))).

337. *See Aramony III*, 191 F.3d 140, 154 n.7 (2d Cir. 1999) (discussing the causation and damages elements for the breach).

338. Unger v. Paul Weiss Rifkind Wharton & Garrison, 696 N.Y.S.2d 36, 37 (App. Div. 1999) (affirming dismissal of a conflict of interest claim against an attorney for his failure to show proximate causation); *accord* Tolmosova v. Umarova, No. 14697/03, 2012 WL 4825102, at *4–5 (N.Y. Sup. Ct. Oct. 1, 2012) (dismissing the plaintiff's complaint, in part, because she did not show malpractice was the cause of damages).

339. RESTITUTION & UNJUST ENRICHMENT § 43 ("Gain resulting from breach of fiduciary duty is a prime example of unjust enrichment that the law of restitution condemns, and one function of the rule of this section is to exclude the possibility of profit from this kind of wrongdoing.").

remedies in equity, the principal needs to identify the object of the remedy: the assets or funds to be deemed a constructive trust; the revenues or profits to be disgorged; or the compensation to be forfeited.[340] Once the principal satisfies this initial requirement, the burden shifts to the fiduciary to disprove the identification, show which portions of the assets or revenues do not apply, and determine what offsets, if any, should be applied.[341] The burden shifts under the law in equity because it is assumed that the fiduciary generally has better access to all relevant information.[342] In the case of compensation forfeiture, the principal needs to identify all applicable compensation and the period of disloyalty outlined by the fiduciary's disloyal acts.[343] In regard to conflicted transactions, once the principal adequately identifies the transaction, the burden shifts to the fiduciary to prove the entire fairness of the transaction.[344]

The D.C. District Court recently held, in *National Railroad Passenger Corp.*

340. *See id.* § 51 reporter's note b (discussing the logic of tracing assets, profits, or other interests that relate to the wrong that merits restitution).

341. *See* C&B Sales & Serv., Inc. v. McDonald, 177 F.3d 384, 387 (5th Cir. 1999) (asserting the burden to establish the defendant's revenues falls on the plaintiff, while the defendant bears the burden of proving its costs under a "reasonable approximation" standard); Otto v. Niles (*In re* Niles), 106 F.3d 1456, 1462 (9th Cir. 1997) (requiring fiduciaries to provide an accounting "once the principal has shown that funds have been entrusted to the fiduciary and not paid over or otherwise accounted for," which "reinforces the substantive policies behind fiduciary law by ensuring that fiduciaries will perform their obligations faithfully and with care"); Clancy v. Coyne, 244 F. Supp. 2d 894, 897–98 (N.D. Ill. 2002) (placing the burden of proof on the defendant–trustee to show that comingled funds were separate from the estate); McClung v. Smith, 870 F. Supp. 1384, 1400–01 (E.D. Va. 1994) (acknowledging accounting places the burden of proof on the agent), *aff'd per curiam in part*, *remanded in part on other grounds*, Nos. 95-1106, 95-1187, 1996 WL 334470 (4th Cir. 1996); Wilz v. Flournoy, 228 S.W.3d 674, 676 (Tex. 2007) (per curiam) (explaining the party "seeking to impose a constructive trust has the initial burden of tracing funds to the specific property sought to be recovered," and if that burden is met, all of the property "will be treated as subject to the trust, except in so far as the trustee may be able to distinguish and separate that which is his own" (citation omitted) (quoting Eaton v. Husted, 172 S.W.2d 493, 498–99 (Tex. 1943))). The plaintiff is, of course, required to trace the revenues of the defendant back to the defendant's wrongdoing. *See* Taylor v. Meirick, 712 F.2d 1112, 1122 (7th Cir. 1983) (providing as an example: "If General Motors were to steal your copyright and put it in a sales brochure, you could not just put a copy of General Motors' corporate income tax return in the record and rest your case for an award of infringer's profits.").

342. RESTITUTION & UNJUST ENRICHMENT § 51(5)(d) (stating a claimant seeking disgorgement of profit bears the burden of proving at least an estimate of the amount of wrongful profit).

343. *E.g.*, Enstar Grp., Inc. v. Grassgreen, 812 F. Supp. 1562, 1571–73 (M.D. Ala. 1993) (analyzing the recovery "because the evidence failed to establish the pay periods in which disloyalty had occurred or the compensation paid for those periods" (citing Simulation Sys. Techs. v. Oldham, 634 A.2d 1034, 1037 (N.J. Super. Ct. App. Div. 1993))).

344. *Clancy*, 244 F. Supp. 2d at 897 (charging the defendant–trustee with proving the absence of a wrongdoing).

v. Veolia Transportation Services,[345] that the defendant is free to refute the assumed causation.[346] In that case, the plaintiff, Amtrak, alleged its competitor, Veolia, aided and assisted three of Amtrak's employees in breaching their fiduciary duty, which enabled Veolia to gain a lucrative project that Amtrak regarded as its own opportunity.[347] Since the employees did find employment with the competitor, and the competitor did gain the project Amtrak had planned to capture, the court held Amtrak did not have to prove it otherwise would have gained the project.[348] The court explained that the law assumes the causation,[349] but the competitor, who was being sued for joint liability with the ex-employee, is free to try to prove it would have gained the project even if the ex-employees had not left the employer.[350] The jury found Veolia did not proximately cause Amtrak to lose the contract, and Veolia, therefore, overcame the assumption and disproved causation.[351]

It is not uncommon for a court to issue an injunction, such as a disqualification order, based on the fear that a fiduciary is likely to breach his fiduciary duty.[352] The proverbial "near-miss" in terms of actual damage tends to be regarded as a "hit." On the other hand, courts occasionally hold that a breach or act of disloyalty was insignificant or

345. Nat'l R.R. Passenger Corp. v. Veolia Transp. Servs., Inc., 886 F. Supp. 2d 14 (D.D.C. 2012).

346. The court notes, because "[t]he purpose of disgorgement [of past and future profits] is remedial," it has the discretion to deny the remedy where it appears it would be "unacceptably punitive." *Id.* at 19 (citing RESTITUTION & UNJUST ENRICHMENT § 51).

347. *Id.* at 16.

348. *Id.* at 18 ("[I]t is not a condition of liability that, absent the disloyalty, [Amtrak] would either have won the contract or made a profit." (citing RESTITUTION & UNJUST ENRICHMENT § 43 cmt. d, illus. 12); *see also* 2 DOBBS, *supra* note 6, § 10.4, at 667 (noting the beneficiary is only required to prove "disloyalty[,] and that is enough to operate as a defense on the contract or as grounds for restitution").

349. *Nat'l R.R. Passenger Corp.*, 886 F. Supp. 2d at 18.

350. Relying on the language of the Restatement (Third) of Restitution and Unjust Enrichment, the court notes:

> The award of disgorgement . . . rests on 'an implicit judgment that the claimant, rather than the wrongdoer, should . . . obtain the benefit of the favorable market conditions, acumen, or luck, as the case may be.' When a court finds the profits are 'the product of legitimate contributions by the defendant that should not, in justice, be awarded to the claimant,' it may deny them as 'too remote' to warrant disgorgement.

Id. at 20 (quoting RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 51 cmt. f (AM. LAW INST. 2011)).

351. *Id.* at 18.

352. *See* Maritrans GP Inc. v. Pepper, Hamilton & Scheetz, 602 A.2d 1277, 1287 (Pa. 1992) ("Damages might later be obtained for breach of fiduciary duties and a confidential relationship, but that remedy would be inadequate to correct the harm that could be prevented by injunctive relief.").

insubstantial and that the trial judge's equitable discretion includes the authority to deny any forfeiture.[353]

IV. FORFEITURE

"Most generalizations about restitution are trustworthy only so long as they are not very meaningful, and meaningful only so long as they are not very trustworthy."[354]

A. *Origins and Foundations for Forfeiture*

Compensation forfeiture is sometimes equated to the faithless servant doctrine, which has been traced back to two New York cases in the 1880s.[355] Alternatively, the Restatement (Second) of Agency has been credited as a key source of supporting principles for forfeiture. Both are important, but they are largely reflections of the law in equity and public policy, which has been denying compensation for fiduciaries since the 1600s.[356] The law in equity on compensation forfeiture is found in fee disputes for estates or trusts in probate court,[357] in bankruptcy court

353. *See Nat'l R.R. Passenger Corp.*, 886 F. Supp. 2d at 19 ("When 'liability for the profits so designated would be unacceptably punitive, being unnecessary to accomplish the object of the disgorgement remedy in restitution,' courts may deny disgorgement, even if some level of attribution exists." (quoting RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 51 cmt. f (AM. LAW INST. 2011))); *In re* Marriage of Pagano, 607 N.E.2d 1242, 1249–50 (Ill. 1992) (reaffirming it is within the court's discretion to award any equitable remedies in a breach of fiduciary duty case).

354. 1 DOBBS, *supra* note 6, § 4.1, at 551.

355. *See* Murray v. Beard, 7 N.E. 553, 554 (N.Y. 1886) (concluding "[a]n agent is held to the [upmost good faith] in his dealings with his principal"); Turner v. Konwenhoven, 2 N.E. 637, 639 (N.Y. 1885) (explaining "[f]lagrant acts of dishonesty or crime which seriously affect the master's interest . . . [could] bar . . . recovery of wages"). Numerous publications have explored the facets of faithless servant doctrine. *E.g.*, Barbara J. Van Arsdale, *Application of "Faithless Servant Doctrine"*, 24 A.L.R. 6th 399, 407 (2007) (indicating states with two or more cases relating to the doctrine include Illinois, Kansas, Kentucky, Massachusetts, New York, Ohio, South Carolina, and West Virginia); Joseph T. Bockrath, *Liability of Corporate Officer or Director for Commission or Compensation Received from Third Person in Connection with That Person's Transaction with Corporation*, 47 A.L.R. 3d 373 (1973) (asserting there is a fundamental fiduciary relationship that exists between a corporation and the people who are in charge of it); Charles A. Sullivan, *Mastering the Faithless Servant?: Reconciling Employment Law, Contract Law, and Fiduciary Duty*, 2011 WIS. L. REV. 777, 780 (recognizing faithlessness is a breach of duty of the fiduciary nature and could entitle the principal to additional remedies).

356. Silbiger v. Prudence Bonds Corp., 180 F.2d 917, 920–21 (2d Cir. 1950) ("Certainly by the beginning of the Seventeenth Century it had become a common-place that an attorney must not represent opposed interests; and the usual consequence has been that he is debarred from receiving any fee from either, no matter how successful his labors." (footnote omitted) (citing Shire v. King (1603) 80 Eng. Rep. 24 (depicting the concept of faithfulness of a servant to its master was recognized during the reign of Elizabeth I))).

357. Wolf v. Weinstein, 372 U.S. 633, 641 (1963) ("These decisions found even in the general

hearings on compensation for all professionals,[358] and in claims against fiduciaries, such as agents[359] and lawyers.[360]

Compensation forfeiture finds its origins in the law in equity because courts in equity were the only courts that provided jurisdiction for claims of breach of fiduciary duty (originally for trusts).[361] A review of the early American opinions on compensation forfeiture reveals the rationale behind the remedy was based in public policy,[362] which remains a high priority for the law in equity today.[363]

terms of the statute the embodiment of 'ancient equity rules governing the conduct of trustees, including deprivation of compensation where there is a departure from those rules.'" (quoting *In re* Republic Gas Corp., 35 F. Supp. 300, 305 (1936))).

358. *E.g.*, *id.* at 641 (recognizing, in the context of a bankruptcy proceeding, the "historic maxim of equity that a fiduciary may not receive compensation for services tainted by disloyalty or conflict of interest").

359. *See* Shaeffer v. Blair, 149 U.S. 248, 258 (1893) (expressing the "fraudulent misconduct proved against [the agent] deprived him of the right to the stipulated commissions"); Wadsworth v. Adams, 138 U.S. 380, 388 (1891) (holding the agent who breached his duty "abused the confidence reposed in him, and thereby lost the right to claim the stipulated compensation . . . or any other sum").

360. *See* Denver v. Roane, 99 U.S. 355, 360–61 (1879) (concluding an attorney was not entitled to share in the compensation for a case because, when he deserted the case, he breached a duty to his partners); *Silbiger*, 180 F.2d at 920–21 (2d Cir. 1950) (recognizing fee forfeiture for attorneys as a remedy in equity as far back as the 1600s (citing Shire v. King (1603) 80 Eng. Rep. 24)).

361. *In re* Evangelist, 760 F.2d 27, 29 (1st Cir. 1985) ("Actions for breach of fiduciary duty, historically speaking, are almost uniformly actions 'in equity'—carrying with them no right to trial by jury."); *see also* 1 DOBBS, *supra* note 6, § 5.18(3), at 935 ("Because equity created the substantive rights against fiduciaries, equity has always taken jurisdiction in claims against them . . . .").

362. Weil v. Neary, 278 U.S. 160, 173 (1929) (voiding a contract for violating public policy despite the outcome "because [it] tend[s] to produce . . . disloyalty by agents and trustees"); Anderson Cotton Mills v. Royal Mfg. Co., 20 S.E.2d 818, 824 (N.C. 1942) ("In selling to itself, the defendant attempted to act in the double capacity of agent and purchaser—a combination so incompatible and noxious to the fundamental rule of loyalty demanded of an agent to his principal, acting as a fiduciary, as to be intolerable to public policy."); *see also* Steinmetz v. Kern, 32 N.E.2d 151, 154 (Ill. 1941) ("[I]t makes no difference whether the result of the agent's conduct is injurious to the principal or not, as the misconduct of the agent affects the contract from considerations of public policy rather than of injury to the principal." (citation omitted)).

363. *See In re* Marriage of Pagano, 607 N.E.2d 1242, 1250 (Ill. 1992) ("While the breach may be so egregious as to require the forfeiture of compensation by the fiduciary as a matter of public policy, such will not always be the case." (citation omitted)); *see also* Moses v. McGarvey, 614 P.2d 1363, 1372 (Alaska 1980) ("It is well established that an attorney, disqualified on conflict-of-interest grounds, generally is barred as a matter of public policy from receiving any fee from either of the opposed interests."), *rev'd*, No. 6095, 1982 WL 889007 (Alaska Sept. 17, 1982); Evans & Luptak, PLC v. Lizza, 650 N.W.2d 364, 368, 369 (Mich. Ct. App. 2002) (agreeing with the defendants argument that the contact at issue was unethical and unenforceable because it violated public policy in Michigan); Buckingham, Doolittle & Burroughs, LLP v. Bonasera, 157 Ohio Misc.2d 1, 2010-Ohio-1677, 926 N.E.2d 375, ¶ 54 (C.P.) ("Further, as public policy mandates, an employee cannot be compensated for his own deceit or wrongdoing." (quoting Roberto v. Brown Cty. Gen. Hosp., 571 N.E.2d 467, 469 (Ohio Ct. App. 1989))).

Three main rationales have traditionally driven forfeiture. First, the agreement for the principal to pay the fiduciary has been held to be void or unenforceable once the fiduciary's disloyalty has been proven.[364]

Second, loyalty of the agent to the principal is implied in the fiduciary relationship, which has been held to apply as a condition precedent.[365] That the agent or employee was present at work at all relevant times and even accomplished his assigned duties without failure was regarded as irrelevant to the later discovery of various forms of disloyalty.[366] Loyalty in and of itself is regarded as a critical component of the fiduciary's service. Without continuous loyalty the fiduciary's services are heavily discounted or ignored.[367]

364. *See Wadsworth*, 138 U.S. at 388 ("He abused the confidence reposed in him, and thereby lost the right to claim the stipulated compensation."); Fish v. Leser, 69 Ill. 394, 400 (1873) (refusing to enforce a contract for the sale of real estate because "[the] agent was employed to buy as well as to sell"); Arnold v. Brown, 41 Mass. (24 Pick.) 89, 96-97 (1832) (holding a conflicted transaction is of no effect because the assent of two minds is essential to a contract of sale); Raisin v. Clark, 41 Md. 158, 160–61 (1874) (forbidding an action founded on a contract where "an agent of the vendor[,] whilst that employment continues, assumes the essentially inconsistent and repugnant relation of agent for the purchaser"); Plotner v. Chillson & Chillson, 95 P. 775, 777 (Okla. 1908) (holding anything short of unswerving loyalty "violated the contract existing between them and forfeited their right to compensation, whether the same was to be paid as commission when the land was bought or 'net profits' when the land was sold").

365. *See Wadsworth*, 138 U.S. at 387 ("It was a condition precedent to his right to such compensation that the services he undertook to render should be faithfully performed."); Rockefeller v. Grabow, 39 P.3d 577, 582 (Idaho 2001) (stating fulfilling one's fiduciary duties is a condition precedent to compensation), *aff'd*, 82 P.3d 450 (Idaho 2003); *Plotner*, 95 P. at 777 (requiring unwavering loyalty by an agent to have a right to compensation); Burrow v. Arce, 997 S.W.2d 229, 240 n.37 (Tex. 1999) ("[T]he breach of the [lawyer's] duty of loyalty is the harm, and the client is not required to prove causation or specific injury." (quoting 1 GEOFFREY C. HAZARD, JR. & W. WILLIAM HODES, THE LAW OF LAWYERING § 1.5:108 (2d ed. Supp. 1998))); Sutherland v. Guthrie, 103 S.E. 298, 301 (W. Va. 1920) ("[I]t is often said that a loyal performance is a condition precedent to the right to recover compensation, and it has been held in many cases that, . . . [the agent] will not be entitled to any compensation for his services." (quoting 1 FLOYD R. MECHEM, A TREATISE ON THE LAW OF AGENCY § 1588, at 1188 (2d ed. 1914))).

366. *See* United States *ex rel.* Rural Util. Serv. v. Schilling (*In re* Big Rivers Elec. Corp.), 355 F.3d 415, 437 (6th Cir. 2004) (expressing, regardless of efforts to benefit the bankruptcy estate, the high price of disloyalty remains harsh and unforgiving).

367. Wolf v. Weinstein, 372 U.S. 633, 642 (1963) ("[T]he general statutory authorization in the Bankruptcy Act for 'reasonable' compensation for services 'necessarily implies loyal and disinterested service in the interest of those for whom the claimant purported to act.'" (quoting Woods v. City Nat'l Bank & Tr. Co. of Chi., 312 U.S. 262, 268 (1941))); Heyman v. Kline, 344 F. Supp. 1110, 1114 (D. Conn. 1970) ("[T]here is an implied condition that the servant will perform the duties incident to his employment honestly[] and will do nothing injurious to his employer's interest, and if he proves radically unfaithful to his trust or is guilty of gross misconduct[,] he forfeits all right to compensation." (quoting Breen v. Larson Coll., 75 A.2d 39, 42 (Conn. 1950))), *rev'd on other grounds*, 456 F.2d 123 (2d Cir. 1972); Foley v. Am. Elec. Power, 425 F. Supp. 2d 863, 873 (S.D. Ohio 2006) ("[D]ishonesty and disloyalty on the part of an employee which permeates his service to his employer

The first two rationales would support a claim for breach of contract or the assertion that the agency contract is void under contract law,[368] but they do not explain why the agent's claim for quantum meruit for past services must fail unless a judge is willing to hold an unfaithful agent's services are worthless as a matter of law. Thus, the third rationale of denying unjust enrichment to an unfaithful agent is necessary to explain the normal practice of full forfeiture over the period of disloyalty.[369]

While it could be argued that forfeiture has a sufficient basis in contract law to resemble a remedy at law,[370] the stronger position remains that forfeiture is a remedy in equity that resembles disgorgement as they both share the driving rationale of denying unjust enrichment to a disloyal fiduciary, which is the third rationale. The role or goal for disgorgement, however, is also mixed among compensation, punishment, and deterrence.[371] Similar in some respects to punitive damages, it can

will deprive him of his entire agreed compensation, due to the failure of such an employee to give the stipulated consideration for the agreed compensation." (quoting Roberto v. Brown Cty. Gen. Hosp., 571 N.E.2d 467, 469 (Ohio Ct. App. 1989))); *see also* Gemini Networks, Inc. v. Nofs, No. CV030824652, 2004 WL 113622, at *1 (Conn. Super. Ct. Jan. 8, 2004) ("[A] number of courts in other states have recognized the basis for return of compensation is 'not in the theory of a penalty[] but in the theory that payment is not due for services not properly rendered.'" (quoting Lydia Pinkham Med. Co. v. Gove, 20 N.E.2d 482, 486 (Mass. 1939))).

368. *See generally* RESTATEMENT (SECOND) OF CONTRACTS § 178 (AM. LAW INST. 1981) (explaining when a term is unenforceable on grounds of public policy); *id.* § 225 (addressing the effects of the non-occurrence of a condition); *id.* § 229 ("To the extent that the non-occurrence of a condition would cause disproportionate forfeiture, a court may excuse the non-occurrence of that condition unless its occurrence was a material part of the agreed exchange.").

369. *See* Blackburn & Co. v. Park, 357 F.2d 525, 526–27 (2d Cir. 1966) (per curiam) ("An agent that has thus disregarded its principal's interests cannot recover for services rendered."); Bryant v. Lewis, 27 S.W.2d 604, 608 (Tex. Civ. App.—Austin 1930, writ dism'd w.o.j.) (affirming a decision that unintentional conflict precluded the lawyer's plea for quantum meruit); *see also* Sullivan, *supra* note 355, at 779 ("[U]nder the faithless servant rule, agreed compensation otherwise earned is forfeited, and, perhaps more surprisingly, the servant is denied quantum meruit recovery for the value of any faithful services he might have rendered." (footnote omitted)).

370. *See* Advanced Nano Coatings, Inc. v. Hanafin, 556 F. App'x. 316, 318–21 (5th Cir. 2014) (affirming an award of $342,117 for breach of contract, which amounts to 100% of the fiduciary's compensation during the period of disloyalty and the plaintiff's lost profits for breach of fiduciary duty); McGowan & Co. v. Bogan (*Bogan I*), 93 F. Supp. 3d 624, 630 (S.D. Tex. 2015) (denying the defendant's motion for summary judgment against a claim under Ohio law for breach of contract for lost profits, compensation for the employee during the period of disloyal competition, and other out-of-pocket cash expenses).

371. *See* Fair v. Bakhtiari, 125 Cal. Rptr. 3d 765, 779 (Ct. App. 2011) (noting forfeiture serves three purposes: (1) it deters misconduct; (2) it prevents unjust enrichment; and (3) it compensates for the decreased value of tainted representation); Ulico Cas. Co. v. Wilson, Elser, Moskowitz, Edelman & Dicker, 843 N.Y.S.2d 749, 762 (Sup. Ct. 2007) ("This is because the function of such an action . . . is not merely to compensate the plaintiff for wrongs committed by the defendant but . . . to prevent them, by removing from agents and trustees all inducement to attempt dealing for their own

punish[372] and deter[373] at the same time. Thus, a defendant who is held liable for breach of fiduciary duty is ordered to disgorge any profits he received that he cannot otherwise prove were not the result of his unjust acts.[374]

Compensation forfeiture operates as either a shield[375] or a sword.[376] It

benefit . . . ." (quoting Diamond v. Oreamuno, 248 N.E.2d 910 (N.Y. 1969))).

372. *See* Rubber Co. v. Goodyear, 76 U.S. (9 Wall.) 788, 804 (1870) ("The rule . . . . compensates one party and punishes the other[,] making the wrong-doer liable for actual, not possible, gains. The controlling consideration is that he shall not profit by his wrong."); *see also* Snepp v. United States, 444 U.S. 507, 515–16 (1980) (per curiam) (explaining constructive trust remedies "conform[] relief to the dimensions of the wrong. . . . [S]ince the remedy reaches only funds attributable to the breach, it cannot saddle the [fiduciary] with exemplary damages out of all proportion to his gain"); Nat'l R.R. Passenger Corp. v. Veolia Transp. Servs., Inc., 886 F. Supp. 2d 14, 19–20 (D.D.C. 2012) ("When 'liability for the profits . . . would be unacceptably punitive . . . courts may deny disgorgement.'" (citing RESTATEMENT (THIRD) OF RESTITUTION § 51 cmt. f (AM. LAW INST. 2011))); Owen v. Shelton, 277 S.E.2d 189, 192 (Va. 1981) ("The purpose of the rule is more prophylactic than remedial; it is applied, not to compensate the principal for an injury, but rather to discipline the fiduciary in the conduct of the office entrusted to him."). However, not all courts agree with this remedy being treated as a punitive one; see Justice White's dissent in *Mertens v. Hewitt*:

> In crafting a remedy for a breach of trust the exclusive aim of the common-law equity courts was to make the victim whole, 'endeavor[ing] as far as possible to replace the parties in the same situation as they would have been in, if no breach of trust had been committed.' Historically, punitive damages were unavailable in any equitable action on the theory that 'the Court of Chancery as the Equity Court is a court of conscience and will permit only what is just and right with no element of vengeance.'

Mertens v. Hewitt Assocs., 508 U.S. 248, 270 n.5 (1993) (White, J., dissenting) (alteration in original) (citation omitted) (first quoting JAMES HILL, A PRACTICAL TREATISE ON THE LAW RELATING TO TRUSTEES 539 (Phila., T. & J.W. Johnson & Co. 1867); and then quoting Beals v. Wash. Int'l, Inc. 386 A.2d 1156, 1159 (Del. Ch. 1978)); *see also Nat'l R.R. Passenger Corp.*, 886 F. Supp. 2d at 19 ("The purpose of disgorgement is remedial, rather than punitive[,] and it 'is meant to provide just compensation for the wrong, not to impose a penalty; it is given in accordance with the principles governing equity jurisdiction, not to inflict punishment but to prevent an unjust enrichment.'" (citation omitted) (quoting *In re* Estate of Corriea, 719 A.2d 1234, 1240 (D.C. 1998))).

373. *See* Woods v. City Nat'l Bank & Tr. Co. of Chi., 312 U.S. 262, 268 (1941) ("What is struck at in the refusal to enforce contracts of this kind is not only actual evil results but their tendency to evil in other cases." (quoting Weil v. Neary, 278 U.S. 160, 173 (1929))); United States v. Carter, 217 U.S. 286, 306 (1910) (noting, because agents are in a position to conceal their frauds, "[i]t would be a dangerous precedent to lay down as law that unless some affirmative fraud or loss can be shown, the agent may hold on to any secret benefit he may be able to make out of his agency"); Hendry v. Pelland, 73 F.3d 397, 402 (D.C. Cir. 1996) ("Forfeiture of legal fees . . . . deters attorney misconduct, a goal worth furthering regardless of whether a particular client has been harmed.").

374. Similarly, the court's orders are scrutinized to avoid unjustly enriching the plaintiff. *See* Charles E. Rounds, Jr., *Relief for IP Rights Infringement Is Primarily Equitable: How American Legal Education Is Short-Changing the 21st Century Corporate Litigator*, 26 SANTA CLARA COMPUTER & HIGH TECH. L.J. 313, 349 (2010) ("The court in equity is loath to fashion a remedy that leaves either party unjustly enriched.").

375. *Kozlowski I*, 756 F. Supp. 2d 553, 564 (S.D.N.Y. 2010) (noting "[t]he 'faithless servant

appears most of the early opinions on forfeiture relate more to the shield function, acting to deny payment for fiduciary or agent compensation.[377] This can be a two-step process in which, first, the principal pursues self-help by terminating the relationship for cause and refusing to pay any compensation; and second, if necessary, the principal answers the fiduciary's collection action or suit for breach of contract with an affirmative defense or counterclaim for disloyalty.[378] In *Aramony*, the forfeiture action against Aramony was brought as a counterclaim against his action to confirm his retirement benefits, which was filed four years after his termination.[379] Given the statute of limitations, however, the counterclaim is less effective than the affirmative defense. If the principal waits to see if the fiduciary will try to collect his compensation, the amount of forfeiture will decline as the statute applies, just as it did in UWA's

doctrine,' used as a sword in [the principal's] claims, may also be used as a shield to [the agent's] counterclaims. . . . [Thus, the principal] has no duty to honor compensation agreements made during [the agent's] period of disloyalty"); *see also* Gammon v. Hodes, No. 03-13-00124-CV, 2015 WL 1882274, at *1 (Tex. App.—Austin Apr. 24, 2015, no pet.) (affirming a take nothing judgment for a lawyer's collection action, awarding forfeiture of additional $23,279 of paid lawyer's fees, and denying a lawyer's claim for quantum meruit due to the breach of fiduciary duty).

376. Shoemake v. Ferrer, 225 P.3d 990, 994 (Wash. 2010) ("It should make no difference whether the lawsuit arises when the lawyer sues for fees and the client defends on the basis of legal malpractice or when the client brings an action for legal malpractice in the first instance.").

377. *See Hendry*, 73 F.3d at 403 ("[C]lients may defend a claim by their lawyer for unpaid legal fees by proving that their attorney breached a fiduciary duty.").

378. *See id.* ("Because the [employers] presented sufficient evidence for a jury to find that [the employee] violated his fiduciary duty, the district court erred in prohibiting them from using this argument as a defense to the counterclaim."); Slosberg v. Callahan Oil Co., 7 A.2d 853, 855 (Conn. 1939) ("In view of the fiduciary character of the office of president no authority is needed to support the defendant's claim. . . . By the conduct described, the plaintiff forfeited any claim to compensation which might otherwise be due." (citations omitted)); Evans & Luptak, PLC v. Lizza, 650 N.W.2d 364, 368 (Mich. Ct. App. 2002) ("Rather, defendants have simply defended a cause of action brought by plaintiff raising as a defense that the alleged contract is unethical because it violates our public policy as expressed in the Michigan Rules of Professional Conduct. We agree with defendants."); Zakibe v. Ahrens & McCarron, Inc., 28 S.W.3d 373, 385 (Mo. Ct. App. 2000) ("Breach of fiduciary duty also constitutes a defense to an action by the agent against the principal for compensation for services. Because of the fiduciary relationship, fiduciary principles modify any contract between the parties. This allows the breach of fiduciary duty to give rise to claims in tort, as well as contract, and to be pleaded as a defense to a contractual claim for compensation." (citations omitted)); Burrow v. Arce, 997 S.W.2d 229, 244 (Tex. 1999) (stating one form of forfeiture is as a "defense of an agent's claim for compensation"); RESTATEMENT (THIRD) OF AGENCY § 8.01 cmt. d. (AM. LAW INST. 2006) ("The availability of forfeiture is not limited to its use as a defense to an agent's claim for compensation.").

379. *See generally Aramony II*, 28 F. Supp. 2d 147 (S.D.N.Y. 1998), *aff'd in part*, *rev'd in part sub nom. Aramony III*, 191 F.3d 140 (2d Cir. 1999) (hearing the counterclaims of UWA against Aramony for fraud and breach of fiduciary duties).

claim.[380]

One issue that occasionally arises in relation to compensation forfeiture is whether an award of compensation forfeiture is covered under professional liability insurance policies, especially legal malpractice policies. The same issue has come up in regard to disgorgement with mixed results, but its connection to compensation forfeiture appears to occur more frequently and often against coverage.[381]

B. *Damages at Law or Remedy in Equity?*

Determining the nature of a cause of action as one in law or in equity is an inexact process that is especially important when the right to a jury trial or injunctive relief is contested.[382] To determine whether a jury trial was required, the recent case, *Client Funding Solutions Corp. v. Crim*,[383] had to evaluate the nature of a claim that sought three remedies (compensatory damages, compensation forfeiture, and punitive damages) to determine whether the gist of the relief sought was in equity or at law.[384] One rule of thumb, for example, is to consider remedies that seek strictly monetary relief as remedies at law and remedies that require specific orders or the exercise of a court's in personam authority as remedies in equity. [385] In

380. *See id.* at 175 (limiting UWA's recovery of damages, including compensation forfeiture, to those occurred within the applicable statutory of limitations period).

381. *See* Level 3 Commc'ns, Inc. v. Fed. Ins. Co., 272 F.3d 908, 910–11 (7th Cir. 2001) ("[A] 'loss' within the meaning of an insurance contract does not include the restoration of an ill-gotten gain . . . ."); Republic W. Ins. Co. v. Spierer, Woodward, Willens, Denis & Furstman, 68 F.3d 347, 351–52 (9th Cir. 1995) (holding an attorney's required disgorgement to the court of fees not properly earned due to disabling conflict of interest was not "damages" for which the insurance policy provided coverage); Burlington Ins. Co. v. Devdhara, No. C09-00421 SBA, 2010 WL 3749301, at *11 (N.D. Cal. Sept. 23, 2010) (finding claims for injunctive relief and disgorgement of unlawfully collected rent sought "equitable relief[,] . . . [not] 'damages' that can be covered by a liability policy"); Haines v. St. Paul Fire & Marine Ins., 428 F. Supp. 435, 439–41 (D. Md. 1977) (concluding a law firm's professional liability insurance did not cover SEC action seeking a judgment requiring the firm to disgorge attorneys' fees); John M. O'Quinn PC v. Nat'l Union Fire Ins. Co. of Pittsburgh, 33 F. Supp. 3d 756, 774 (S.D. Tex. 2014) (affirming an arbitration panel's denial of insurance coverage because improper deductions, "together with prejudgment interest, attorneys' fees, and the forfeiture of $25 million in fees received [was] sufficient to satisfy the 'profit or advantage to which [it] was not legally entitled' exclusion"). For additional information, see generally Katherine C. Skilling, Comment, *Coverage for Ill-Gotten Gains?: Discussing the (Un)Insurability of Restitution and Disgorgement*, 72 WASH & LEE L. REV. 1077 (2015).

382. *E.g.*, Design Strategy, Inc. v. Davis, 469 F.3d 284, 299 (2d Cir. 2006) (distinguishing a claim for lost profits as legal and a claim for disgorgement as equitable).

383. Client Funding Sols. Corp. v. Crim, 943 F. Supp. 2d 849 (N.D. Ill. 2013).

384. *Id.* at 858.

385. *Id.* ("As a general matter, though, legal remedies traditionally involve money damages, while '[e]quitable remedies, by contrast, are typically coercive[] and are enforceable directly on the person or thing to which they are directed.'" (1st alteration in original) (quoting Int'l Fin. Servs. Corp.

Crim, the court pursued a two-prong test that inquired into (1) the historical nature of the remedies and, more importantly, (2) the nature of the package of remedies sought.[386] The court found the second prong indeterminate due to the strongly mixed nature of the remedies, but it found the historical nature of a fiduciary claim was definitely in equity, so it denied the jury trial.[387]

Compensation forfeiture is largely regarded as a remedy in equity, but it can also be found in contract law, especially for compensation forfeiture as a defense to a collection action.[388] There is ample precedent to the effect that a conflicted transaction or a representation agreement is void or has been breached by a dual agency.[389] Ignoring the issue of irreparable injury, some courts have rationalized awarding compensation forfeiture as damages based on the argument that if the fiduciary had complied with her duty to disclose her breach, the employer would have fired her; and therefore, the employer has been damaged to the extent it had to pay wages to a disloyal fiduciary.[390] Left unexplained is why benefits to the

v. Chromas Techs. Can., Inc., 356 F.3d 731, 736 (7th Cir. 2004))). *But see id.* at 856–57 ("[T]he fact that disgorgement involves a claim for money does not detract from its equitable nature: in such an action, the court is not awarding damages to which plaintiff is legally entitled but is exercising the chancellor's discretion to prevent unjust enrichment." (alteration in original) (quoting SEC v. Rind, 991 F.2d 1486, 1493 (9th Cir. 1993))). For a further discussion on the terminology of restitution, see Murphy, *supra* note 282, at 1610.

386. *Crim*, 943 F. Supp. 2d at 856.

387. *Id.* at 858 ("In the final analysis, the court found a 'mixed result' under prong two, as the breach of fiduciary duty claims sought 'both legal and equitable relief.' And in resolving the ultimate question of the appropriate finder of fact to resolve those claims, the court concluded that 'the scales tip in favor of Plaintiffs' claims being judged equitable' because '[t]o weigh the factors differently would effectively ignore the historical factor, contrary both to the Seventh Amendment's purpose . . . and to the express holding of [*Granfinanciera v. Nordberg*], that history is to be accorded weight in the balancing." (1st & 2nd alterations in original) (citations omitted) (quoting Cantor v. Perelman, No. Civ.A. 97-586-KAJ, 2006 WL 318666, at *9 (D. Del. Feb. 10, 2006))).

388. *See* Zakibe v. Ahrens & McCarron, Inc., 28 S.W.3d 373, 385 (Mo. Ct. App. 2000) (describing how an agent's breach of fiduciary duty gives rise to claims in contract and tort that may be pled to defend against a claim for compensation).

389. *E.g.*, Riley v. Powell, 665 S.W.2d 578, 581 (Tex. App.—Fort Worth 1984, writ ref'd n.r.e.) ("Whenever an agent breaches his duty to his principal by becoming personally interested in an agency agreement, the contract is voidable at the election of the principal without full knowledge of all the facts surrounding the agent's interest." (quoting Ramsey v. Gordon, 567 S.W.2d 868, 871 (Tex. Civ. App.—Waco 1978, writ ref'd n.r.e.))).

390. *See* HTS, Inc. v. Boley, 954 F. Supp. 2d 927, 955 (D. Ariz. 2013) ("[T]he employee 'supported himself with compensation he received from [his employer] while he plotted against its interests. Had he resigned as soon as he embarked on competition against [his employer], or had . . . [he] disclosed defendants' activities, [his employer] would not have continued to pay him.'" (2nd–4th & 6th alterations in original) (quoting Serv. Emp. Int'l Union v. Colcord, 72 Cal. Rptr. 3d 763, 769 (Ct. App. 2008))); Sunset Acres Motel, Inc. v. Jacobs, 336 S.W.2d 473, 483 (Mo. 1960) ("The theory is, perhaps, that the commission was never rightfully paid under the circumstances, that the money

principal from the agent's endeavors are not credited.

Claims relating to bribes can be pled either at law or in equity as it is now widely accepted that the principal can plead for the bribe as either an unjust enrichment for the employee or as damages (the bribe being a reasonable estimate of the principal's loss from the bribery).[391]

Originally, all claims against trustees and fiduciaries were resolved in courts in equity because common law courts did not recognize trusts or trustees as independent entities.[392] By the time of Justice Story's treatise on equity jurisprudence, only trusts and trustees retained exclusive jurisdiction in equity.[393] Then, as now, claims against non-trustee fiduciaries enjoyed concurrent jurisdiction, which has been subject to the doctrine of irreparable injury since 1616 and requires the claimant who seeks jurisdiction in equity to show her claim would be otherwise irreparably damaged without the help of a court in equity—i.e., that she would not be entitled to an adequate remedy at law for her cause of action based on the particular case facts.[394]

So why isn't irreparability discussed more often in appellate opinions on compensation forfeiture?[395] First, the doctrine is fading in use and has

still belongs to the seller, and that he has been damaged to the extent of the wrongful payment.").

391. *See* Williams Elecs. Games, Inc. v. Garrity, 366 F.3d 569, 576 (7th Cir. 2004) ("The victim of commercial bribery . . . can obtain . . . either the damages . . . or the profits that the bribe yielded. . . ."); *see also* 2 DOBBS, *supra* note 6, § 10.6, at 700 (exploring court treatment of bribes "either as restitution or as damages" (footnote omitted)).

392. *See In re* Evangelist, 760 F.2d 27, 29 (1st Cir. 1985) (mentioning claims for breach of fiduciary duty have historically been actions in equity); *see also* 1 DOBBS, *supra* note 6, § 5.18(3), at 935 ("Because equity created the substantive rights against fiduciaries, equity has always taken jurisdiction in claims against them without regard to the adequacy test.").

393. In his treatise on equity jurisprudence, Justice Story discusses how trusts were "wholly without any cognizance at the common law," and how "the abuses of such trusts and confidences [were] beyond the reach of any legal process," except, in courts of equity. *See* 1 JOSEPH STORY, COMMENTARIES ON EQUITY JURISPRUDENCE § 29, at 20 (Jairus W. Perry ed., Bos., Little, Brown & Co., 12th ed. 1877).

394. The Restatement (Second) of Agency discusses this equitable relief principle:

> A principal does not have an action for an account or other equitable relief against an agent merely because of the existence of the agency relation or because the agent has received something for or from the principal. However, equitable relief may be granted not only when there is no adequate remedy at law, as where an injunction is granted, but also where there is a close fiduciary relation. If the agent is not only an agent[] but also a trustee, as where he is given money to invest for the principal which he invested in his own name, an action for an accounting will ordinarily lie.

RESTATEMENT (SECOND) OF AGENCY § 399 cmt. e (AM. LAW INST. 1958).

395. *But see* Searcy, Denney, Scarola, Barnhart & Shipley, PA. v. Scheller, 629 So.2d 947, 951 (Fla. Dist. Ct. App. 1993) (holding the failure of the trial court to consider the adequacy of legal remedies for the breach before ordering a fee forfeiture was error).

now been rejected by two Restatements.[396] Second, irreparability is much more likely to arise if injunctive relief is in dispute rather than a plea for a monetary remedy in equity.[397] Third, there is no alternative remedy at law for compensation forfeiture. Without an alternative, such forfeiture falls under no adequate remedy at law, which should allow a court in equity to hear the plea and possibly order that remedy.

The degree to which some courts dismiss the issue of jurisdiction or the authority in equity to grant the forfeiture of compensation is revealed in the 2010 opinion, *Tyco International, Ltd. v. Kozlowski*.[398] In *Kozlowski*, Judge Griesa specifically stated he had not determined whether Tyco would suffer an irreparable injury without a remedy in equity for its claims or whether remedies at law offered Tyco an adequate remedy, but he felt free to grant a summary judgment motion for forfeiture of more than $100 million without any consideration of whether forfeiture is a remedy in equity or at law.[399]

The evaluation of whether a cause of action is pled as a remedy in equity or at law is frequently based on examination of the nature of the remedy.[400] In addition to the considerations below, and other traditional considerations, more attention could be focused on the process and procedures sought by the parties to determine the nature of the cause of action:

396. *See* RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 4(2) (AM. LAW INST. 2011) ("A claimant otherwise entitled to a remedy for unjust enrichment, including a remedy originating in equity, need not demonstrate the inadequacy of available remedies at law."); Douglas Laycock, *The Death of the Irreparable Injury Rule*, 103 HARV. L. REV. 687, 692 (1990) ("The Restatement (Second) of Torts dropped the traditional version of the rule from the black letter and condemned it as misleading. . . ."). Laycock goes on noting the "reasons for denying equitable remedies are not derived from the adequacy of the legal remedy or from any general preference for damages. . . . Sometimes there are good reasons to deny legal relief and grant equitable relief instead. But there is no general presumption against equitable remedies." *Id.*

397. Based on prior investigation using word searches, the author found the terms "adequate remedy" or "irreparable injury," in general, were found in less than 5% of the Texas cases that used "unjust enrichment" or "constructive trust" as core terms. George P. Roach, *Rescission in Texas: A Suspect Remedy*, 31 REV. LITIG. 493, 538 n.185 (2012). In contrast, the corresponding range for injunction or mandamus is from 20% to 40%, and similar searches for all U.S. state courts showed comparable distinctions between rescission and injunction or mandamus for the last 110 years. *Id.* at 538.

398. Tyco Int'l, Ltd. v. Kozlowski (*Kozlowski I*), 756 F. Supp. 2d 553 (S.D.N.Y. 2010).

399. *See id.* at 561–62 (granting summary judgment as to the breach of fiduciary duty cause of action).

400. *See* Client Funding Sols. Corp. v. Crim, 943 F. Supp. 2d 849, 856 (N.D. Ill. 2013) ("[W]e examine the remedy sought and determine whether it is legal or equitable in nature." (quoting Granfinanciera, SA v. Nordberg, 492 U.S. 33, 42 (1989))).

- Has the plaintiff pled she was damaged (if not, her action can only survive as a claim in equity);
- Is the plaintiff going to carry the entire burden of proof for damages (if the plaintiff is relying on shifting the burden of proof, her action can only survive as a remedy in equity);
- Which causation standard has the plaintiff pled? Does the plaintiff intend to meet that of minimal, relaxed causation for remedies in equity or the normal, full causation standard for remedies at law?;
- Does the plaintiff intend to present ex post evidence for her remedies measure or will she rely on the ex ante standard for remedies at law? And;
- Does the plaintiff intend to exercise her discretion under the anti-netting rule to pick and choose which breaches of duty are to be included in the ex post results and which are to be rejected and considered as ex ante losses?[401]

C. *Who Is a Fiduciary?*

There are many fine articles on the nature of fiduciary duty and of fiduciaries in general.[402] Professor DeMott, the reporter for the Restatement (Third) of Agency, suggests "[t]he defining or determining criterion should be whether the plaintiff (or claimed beneficiary of a fiduciary duty) would be justified in expecting loyal conduct on the part of an actor and whether the actor's conduct contravened that

401. The anti-netting doctrine is only found in remedies in equity. *See* George P. Roach, *Counting the Beans: Unjust Enrichment and the Defendant's Overhead*, 16 TEX. INTELL. PROP. L.J. 483, 523–26 (2008) (discussing the anti-netting doctrine). "It is useful to take a 'back-bearing' on applications of the anti-netting doctrine. It is an obscure doctrine in measuring unjust enrichment, yet it has appeared as a measurement rule for fiduciary claims, patents, copyrights, trademarks, trade secrets, and federal agency claims." *Id.* (footnotes omitted).

402. For further discussion, see generally J.C. SHEPHERD, THE LAW OF FIDUCIARIES (1981), Gregory S. Alexander, *A Cognitive Theory of Fiduciary Relationships*, 85 CORNELL L. REV. 767 (2000), Margaret M. Blair & Lynn A. Stout, *Trust, Trustworthiness, and the Behavioral Foundations of Corporate Law*, 149 U. PA. L. REV. 1735 (2001), Andrew Burrows, *We Do This at Common Law but That in Equity*, 22 OXFORD J. LEGAL STUD. 1 (2002), Matthew Conaglen, *The Nature and Function of Fiduciary Loyalty*, 121 L.Q. REV. 452 (2005), Deborah A. DeMott, *Breach of Fiduciary Duty: On Justifiable Expectations of Loyalty and Their Consequences*, 48 ARIZ. L. REV. 925 (2006) [hereinafter DeMott, *Breach of Fiduciary Duty*], Deborah A. DeMott, *Beyond Metaphor: An Analysis of Fiduciary Obligation*, 1988 DUKE L.J. 879, Deborah A. DeMott, *Disloyal Agents*, 58 ALA. L. REV. 1049 (2007), Frank H. Easterbrook & Daniel R. Fischel, *Contract and Fiduciary Duty*, 36 J.L. & ECON. 425 (1993), Tamar Frankel, *Fiduciary Duties*, 71 CAL. L. REV. 795 (1983), Lawrence E. Mitchell, *The Death of Fiduciary Duty in Close Corporations*, 138 U. PA. L. REV. 1675 (1990), and Ernest J. Weinrib, *The Fiduciary Obligation*, 25 U. TORONTO L.J. 1 (1975).

expectation."[403] Without pretending to do the subject adequate justice, it might be noted that other suggestions include a relationship based in trust and confidence[404] or a relationship in which the fiduciary is given authority in a consensual agreement.[405]

In forfeiture cases, the key dispute often comes down to the applicable definition of agent as it is generally agreed that agents are fiduciaries.[406] Some state courts hold all employees are agents,[407] while others only include officers and directors,[408] and a third group employs a facts-and-

403. DeMott, *Breach of Fiduciary Duty*, *supra* note 402, at 936.

404. Parham v. Wendy's Co., No. 14-cv-14367-ADB, 2015 WL 1243535, at *7 (D. Mass. Mar. 17, 2015) (stating Massachusetts law includes as fiduciaries: managers and officers as well as other employees who are assigned "a position of 'trust and confidence'"); RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 43 cmt. a (AM. LAW INST. 2011) ("Courts in some jurisdictions distinguish fiduciary obligations in a strict sense . . . from analogous obligations owed by persons, not technically fiduciaries, who nevertheless occupy toward others a 'relation of trust and confidence' as regards the transaction in question.").

405. Stearns v. McGuire, 154 F. App'x. 70, 75 (10th Cir. 2005) ("We conclude that the real estate contract between McGuire and the Staffords is not a written agreement sufficient to transform Stearns from a transaction-broker into a seller's agent. Missing from that document is a manifestation of McGuire's consent for Stearns to serve as his agent." (footnote omitted)); RESTATEMENT (THIRD) OF AGENCY, § 8.01 cmt. b. (AM. LAW INST. 2006) ("The relationship between a principal and an agent is a fiduciary relationship. An agent assents to act subject to the principal's control and on the principal's behalf." (citation omitted)).

406. AGENCY § 8.01 cmt. b. ("The relationship between a principal and an agent is a fiduciary relationship.").

407. *See* Eckard Brandes, Inc. v. Riley, 338 F.3d 1082, 1086 (9th Cir. 2003) ("Nothing in the Restatement indicates, however, that ordinary employees have no duty of loyalty."); Eaton Corp. v. Giere, 971 F.2d 136, 141 (8th Cir. 1992) (holding a product engineer had breached his duty of loyalty when he solicited his employer's customers for himself); Vigoro Indus., Inc. v. Cleveland Chem. Co. of Ark., 866 F. Supp. 1150, 1164 (E.D. Ark. 1994) ("Every employee owes his or her employer a duty of loyalty."), *aff'd in part*, *rev'd on other grounds*, 82 F.3d 785 (8th Cir. 1996); Regal–Beloit Corp. v. Drecoll, 955 F. Supp. 849, 858 (N.D. Ill. 1996) (stating a duty of loyalty by employees is owed to "any and all maters within the scope of their agency"); FryeTech, Inc. v. Harris, 46 F. Supp. 2d 1144, 1152 (D. Kan. 1999) (noting an agent or employee is prohibited from doing anything that is "inconsistent with his agency or trust," binding the agent to act with "the utmost good faith and loyalty in the performance of his duties" (quoting Bessman v. Bessman, 520 P.2d 1210, 1217 (Kan. 1974) (demanding a disloyal agent "must account . . . for secret profits . . . [and] forfeit[] his right to compensation for services rendered"))); Green v. H & R Block, Inc., 735 A.2d 1039, 1051 (Md. 1999) (reiterating the decisive test for determining whether a master–servant relationship exists is "whether the employer has the right to control and direct the servant in the performance of his work and in the manner in which the work is to be done" (quoting Chevron, U.S.A., Inc. v. Lesch, 570 A.2d 840, 844 (Md. 1990))); *see also* Leslie Larkin Cooney, *Employee Fiduciary Duties: One Size Does Not Fit All*, 79 MISS. L.J. 853, 870–71 (2010) (discussing the disjunction between agency law in the general sense versus its effects on lower-level employees).

408. United Teachers Assocs. Ins. Co. v. Mackeen & Bailey Inc., 99 F.3d 645, 655 (5th Cir. 1990) (explaining some fiduciary duties in agency relationships are only applicable to officers, directors, and majority shareholders); *Parham*, 2015 WL 1243535, at *7 (noting certain employees are entrusted with confidential information and "hold a position of 'trust and confidence'"); White v.

circumstances test.[409] In a few states, all employees have fiduciary duties, but they are scaled by each employee's position.[410] In Georgia, the agency relationship is provided by statute and is created at the discretion of the employer.[411]

There is concern among some employment law scholars that defining agents to include at-will employees or rank-and-file employees is over inclusive and that compensation forfeiture is too severe.[412] There have

Ransmeier & Spellman, 950 F. Supp. 39, 43 (D.N.H. 1996) ("The defendant's claim, which seeks recovery for acts of an at-will, non-managerial employee, falls outside the scope . . . of any cause of action for breach of the duty of loyalty recognized by the New Hampshire Supreme Court."); Efird v. Clinic of Plastic & Reconstructive Surgery, PA, 147 S.W.3d 208, 221 (Tenn. Ct. App. 2003) (noting, if the agent–doctor "was an officer or director of the Clinic during the period of time in which he was directing patient fees and insurance payments to his separate accounts, his actions would constitute a breach of his fiduciary duties, and the Clinic would be entitled to appropriate damages").

409. *See* E.L. Hamm & Assocs., Inc. v. Sparrow (*In re* Sparrow), 306 B.R. 812 (Bankr. E.D. Va. 2003) (speaking on the bankruptcy code's standard of deeming the existence of a fiduciary duty for employees, the court explains whether an employee has a fiduciary duty rests on whether there was a position of trust in which the employee held); Jet Courier Serv. v. Mulei, 771 P.2d 486, 497 (Colo. 1989) (stating the court should consider the nature of the employment relationship, "the impact or potential impact of the employee's actions on the employer's operations," and the benefit received by the employer during the period of disloyalty); Futch v. McAllister Towing of Georgetown, Inc., 518 S.E.2d 591, 596–97 (S.C. 1999) (stating, in assessing compensation in forfeiture, the court should consider "the nature of the employment relationship, the nature and extent of the employee's services and the breach of duty, the loss or expense caused to the employer by the breach of duty, and the value to the employer of the services properly rendered by the employee"); Johnson v. Brewer & Pritchard, PC, 73 S.W.3d 193, 200 (Tex. 2002) (mentioning it is "impossible to give a definition of the term" fiduciary duties in a way "comprehensive enough to cover all cases"). In *Dalton v. Camp*, the North Carolina Supreme Court describes the fiduciary relationship as follows:

> For a breach of fiduciary duty to exist, there must first be a fiduciary relationship between the parties[,] . . . broadly defined . . . as one in which "there has been a special confidence reposed in one who in equity and good conscience is bound to act in good faith and with due regard to the interests of the one reposing confidence. . . . [and] 'it extends to any possible case in which a fiduciary relation exists in fact, and in which there is confidence reposed on one side, and resulting domination and influence on the other.'"

Dalton v. Camp, 548 S.E.2d 704, 707–08 (N.C. 2001) (4th & 5th alterations in original) (citation omitted) (quoting Patterson v. Strickland, 515 S.E.2d 915, 919 (N.C. Ct. App. 1999).

410. *See* Pride Mobility Prods. Corp. v. Dylewski, No. 3:08-cv-0231, 2009 WL 249356, at *18 (M.D. Pa. Jan. 27, 2009) ("[D]efendants were shareholders, employees, directors, and managers of the plaintiff corporation and clearly owed the plaintiff corporation the fiduciary duties commensurate with their respective positions."); *see also Drecoll*, 955 F. Supp. at 857–58 ("Rather, all employees owe their employers a fiduciary duty of loyalty with respect to any and all matters within the scope of their agency."); Cameco, Inc. v. Gedicke, 724 A.2d 783, 791 (N.J. 1999) (stating a director or officer has higher fiduciary duty than the employee that works on a production line).

411. *See* Cooney, *supra* note 407, at 862 ("Georgia statutes define the agency relationship as arising 'wherever one person, expressly or by implication, authorizes another to act for him or subsequently ratifies the acts of another in his behalf.'" (quoting GA. CODE ANN. § 10-6-1 (2008))).

412. *See* Alan Hyde, *What Should the Proposed Restatement of Employment Law Say About Remedies?*,

been some cases in which forfeiture was seen as an abuse on the margin against non-senior employees to unnecessarily control employees' lives away from the workplace—e.g., by controlling employees' affiliation with a second job[413] or even by restricting employees' free speech rights.[414] *Food Lion, Inc. v. Capital Cities*[415] is one such example where the employer used a claim of disloyalty to restrict an employee's First Amendment rights.[416] At least three states have enacted statutes to protect employees'

16 EMPL. RTS. & EMPLOY. POL'Y J. 497, 508 (2012) ("Many scholars of employment law were surprised at the recent line of New York cases awarding employers who show employee breach of the duty of loyalty all of the employee's compensation from the onset of disloyalty—the so-called 'faithless servant rule.'").

413. *See* JILL RUBERY ET AL., *Blurring the Boundaries to the Employment Relationship: From Single to Multi-employer Relationships*, *in* FRAGMENTING WORK: BLURRING ORGANIZATIONAL BOUNDARIES AND DISORDERING HIERARCHIES 63, 64 (Mick Marchington et al. eds., 2005) ("Where employees of one organization work in environments open to pressure and influence from other employers, the relevance of key notions of . . . loyalty . . . are called into question."); John A. Boyle, *Employee Assistance to an Employer's Competitor, Including Formation of a Competing Business, May Breach the Employee's Duty of Loyalty and Require Forfeiture of Compensation Paid to the Employee During Periods of Disloyalty*—Cameco, Inc. v. Gedicke, *157 N.J. 504, 724 A.2d 783 (1999)*, 30 SETON HALL L. REV. 673, 679 (2000) ("[T]he existence of contractual provisions, such as a noncompete clause or a clause permitting an employee to seek a second source of income, will affect the analysis.").

414. *See* Curran v. Cousins, 509 F.3d 36, 50 (1st Cir. 2007) (holding an employee can violate his or her duty by discrediting the employer's name through posting messages on an internet blog); Grigsby v. Kane, 250 F. Supp. 2d 453, 455 (M.D. Pa. 2003) (finding two former attorneys for Pennsylvania's Bureau of Professional Licensing and Occupational Affairs were properly terminated for speaking out against a new quota system); *see also* Laura DiBiase, *To Blog or Not to Blog?*, AM. BANKR. INST. J., Nov. 2005, at 32 ("Notable companies such as Google Inc. and Starbucks have allegedly fired employees for posting remarks online, including remarks against other employees."); Aaron Kirkland, "*You Got Fired? On Your Day Off?!": Challenging Termination of Employees for Personal Blogging Practices*, 75 UMKC L. REV. 545, 548 (2006) ("According to a recent survey of 294 large U.S. companies, 7.1[%] of companies have terminated an employee for 'violating blog or message board policies in the last twelve months.'"); Konrad Lee, *Anti-employer Blogging: Employee Breach of the Duty of Loyalty and the Procedure for Allowing Discovery of a Blogger's Identity Before Service of Process Is Effected*, 2006 DUKE L. & TECH REV. 0002, ¶ 23, http://scholarship.law.duke.edu/cgi/viewcontent.cgi?article=1148&context=dltr ("While the foregoing illustrates employees who did not realize they were illegally engaging in anti-employer banter, there is still a strong moral obligation to the employer, and the unintentional damage has still been done . . . ."); Tory A. Weigand, *Employee Duty of Loyalty and the Doctrine of Forfeiture*, 42 BOS. B.J., Sept.–Oct. 1998, at 6, 20 ("By definition, the reach of the duty is not limited to trade secrets or transactional transgressions[] but encompasses any conduct of the employee which is inconsistent with the interest of the employer. As such, the potential expanse of the duty's reach remains unchartered.").

415. Food Lion, Inc. v. Capital Cities/ABC, Inc., 951 F. Supp. 1224 (M.D.N.C. 1996).

416. *See id.* at 1233 (holding the grocery store chain had stated a cause of action for disloyalty against television reporters who surreptitiously gained employment to the chain to gather evidence for a planned exposé on the chain's poor meat packing practices). *But see* Dalton v. Camp, 548 S.E.2d 704, 709 (N.C. 2001) (objecting to the holding in *Food Lion* and declaring not all employees are deemed to be fiduciaries).

personal activities.[417]

Without the support of polling or statistics, it nevertheless seems reasonable to posit, while most employees know they should be loyal to their employer and their employer may expect them to be loyal,[418] the vast majority of all employees—salaried and hourly—is not aware of the jeopardy they face from compensation forfeiture for violating the implied duty of loyalty. Employees' vulnerability for a series of foolishly disloyal acts is compounded by the fact that their employer need not prove proximate cause or the intent to be disloyal.[419] Nevertheless, it only seems reasonable to expect some minimum loyalty within the context of an employee's job description: night watchmen have a fiduciary duty to exclude intruders from the company's property, and secretaries have a fiduciary duty to respect the confidentiality of the material that flows across their desks.

D. *Disloyalty*

The following categories, describing the forms of disloyalty, are not all-inclusive, and there is significant overlap among them.

Conflicts: A fiduciary could be considered to be conflicted in any of the following situations: (1) where the fiduciary represents two principals without their informed consent (dual representation);[420] (2) where the

417. *See* COLO. REV. STAT. ANN. § 24-34-402.5 (1) (West 2007) (forbidding an employer from firing "any employee due to that employee's engaging in any lawful activity off the premises of the employer during nonworking hours"); N.Y. LAB. LAW § 201-d(2)(c) (McKinney 2015) (restricting employer termination for an employee's "legal recreational activities outside work hours"); N.D. CENT. CODE § 14-02.4-03 (2013) (forbidding discrimination based on an employee's lawful off-duty activities).

418. This may be sufficient, under Professor DeMott's definition, to justify a fiduciary relation. *See* DeMott, *Breach of Fiduciary Duty*, *supra* note 402, at 936 (defining a fiduciary duty as one that comes into existence when a plaintiff "would be justified in expecting loyal conduct" and when the "actor's conduct contravened that expectation").

419. Hendry v. Pelland, 73 F.3d 397, 401 (D.C. Cir. 1996) (relaxing the standard for proving cause if the remedy sought compensation forfeiture); Arst v. Stifel, Nicolaus & Co., 954 F. Supp. 1483, 1488 (D. Kan. 1997) (holding the plaintiff did not need to show materiality and causation for disgorgement); *see also* DeMott, *Causation in the Fiduciary Realm*, *supra* note 332, at 867–68 (calling the causal standard "a function of the remedy sought by the beneficiary").

420. Wolf v. Weinstein, 372 U.S. 633, 641 (1963) ("The relevant legislative materials leave no doubt that the purpose behind § 249 was to codify the rule of these decisions and to give pervasive effect in Chapter X proceedings to the historic maxim of equity that a fiduciary may not receive compensation for services tainted by disloyalty or conflict of interest."); So v. Suchanek, 670 F.3d 1304, 1310 (D.C. Cir. 2012) (holding an objective observer would have had reasonable doubt about the ability to provide joint representation without limitation from the start); Stearns v. McGuire, 154 F. App'x. 70, 74–75 (10th Cir. 2005) ("When a real estate broker serves as a seller's agent and breaches a fiduciary duty, he 'not only forfeits the commission but also is liable for the full amount

fiduciary, generally a sales agent, agrees to split fees or commissions with the agent for an opposing interest (split fees);[421] (3) where the fiduciary agrees to represent a new client that would conflict with her representation of an existing or prior client (new client);[422] and (4) where the fiduciary enters into a business transaction with the principal after the fiduciary has assumed her role as fiduciary.[423]

The traditional position on conflicted transactions was that conflicted transactions did not occur because any sale takes two parties.[424] Similarly, courts have held retainer agreements for conflicted fiduciaries were unenforceable due to public policy.[425] Normally, courts of equity will not

of' any actual loss suffered by the seller." (citing Moore & Co. v. T-A-L-L, Inc., 792 P.2d 794, 800 n.8 (Colo. 1990))); Kingsley Assoc., Inc. v. Del–Met, Inc., 918 F.2d 1277, 1283 (6th Cir. 1990) ("[T]he law will not permit an agent to act in a dual capacity in which his interest conflicts with his duty, without a full disclosure of the facts to his principal." (quoting Sweeney & Moore, Inc. v. Chapman, 294 N.W. 711, 712–13 (1940))).

421. Weil v. Neary, 278 U.S. 160, 173–74 (1929) (speaking on the evils of splitting fees, the court rather harshly condemned the employee who engaged in this activity); Evans & Luptak, PLC v. Lizza, 650 N.W.2d 364, 369 (Mich. Ct. App. 2002) (holding a contract that provides for a fee-splitting arrangement is unethical and unenforceable). *But see* Allapattah Servs., Inc. v. Exxon Corp., 454 F. Supp. 2d 1185, 1238 (S.D. Fla. 2006) (holding the fee splitting agreement did not warrant full forfeiture because lawyer was instrumental in case).

422. *See In re* Marriage of Newton, 2011 IL App (1st) 090683, ¶ 41 (ordering the forfeiture of fees from an attorney who was first consulted briefly by the ex-husband and later retained by the ex-wife to sue on a complaint for separate maintenance (citing King v. King, 367 N.E.2d 1358, 1360 (Ill. App. Ct. 1977))); Price Waicukauski & Riley, LLC v. Murray, 47 F. Supp. 3d 810, 824 (S.D. Ind. 2014) (finding, while the lawyer should have secured the first client's consent to representation of the second client, no conflict was applicable because the client failed to plead for breach of fiduciary duty).

423. In *Fair v. Bakhtiari*, the court describes its approach in dealing with these fiduciary–principal transactions:

> [S]uch transactions are always scrutinized by courts with jealous care[] and are set aside at the mere instance of the client, unless the attorney can show by extrinsic evidence that his client acted with full knowledge of all the facts connected with such transaction[] and fully understood their effect; and in any attempt by the attorney to enforce an agreement on the part of the client growing out of such transaction, the burden of proof is always upon the attorney to show that the dealing was fair and just[] and that the client was fully advised.

Fair v. Bakhtiari, 125 Cal. Rptr. 3d 765, 778 (Ct. App. 2011) (quoting Felton v. Le Breton, 28 P. 490, 494 (Cal. 1891)).

424. *See* Arnold v. Brown, 41 Mass. (24 Pick.) 89, 96 (1832) ("The assent of two minds is essential to the contract of sale, as well as to every other contract. Hence the action of one person can never change the ownership of property.").

425. *See Weil*, 278 U.S. at 173–74 ("Enforcement of such contracts, when actual evil does not follow, would destroy the safeguards of the law and lessen the prevention of abuses."); Youngman v. DeSoto (*In re* DeSoto), No. 05-29744 DHS, 2010 WL 5093339, at *5–6 (Bankr. D.N.J. Dec. 7, 2010) ("The basic principles . . . have remained largely unchanged for nearly seven decades. . . . Actual conflicting interests are barred[,] and nothing further must be shown to support a complete denial of compensation." (citing Woods v. City Nat'l Bank & Tr. Co. of Chi., 312 U.S. 262, 268 (1941))); Fish

hear the complaints of claimants who are determined to have acted outside public policy.[426]

State courts generally take one of two positions: either the fiduciary must forfeit all fees from the first client[427] or the fiduciary must forfeit the fees from both clients.[428] Of course, there have been a few exceptions,[429] and distinctions have been made between potential conflicts and actual or direct conflicts.[430]

Claims relating to conflicts between existing clients and new clients focus on preventing damage or deterring possible breaches of confidentiality. Injunctive relief is awarded to a lawyer's client if the judge

v. Leser, 69 Ill. 394, 400 (1873) (holding a conflicted contract is unenforceable).

426. *See* Andrew Kull, *Restitution's Outlaws*, 78 CHI.-KENT L. REV. 17, 18 (2003) ("[R]estitution does punish, but it punishes negatively: not by imposing liability on disfavored parties, nor by enhancing the liability to which disfavored parties are subject[] but by denying a restitutionary claim (or counterclaim) to which the disfavored party would otherwise be entitled.").

427. *See* Easley v. Brookline Tr. Co., 256 S.W.2d 983, 989 (Tex. Civ. App.—Amarillo 1952, writ ref'd n.r.e.) ("[A]n attorney cannot serve conflicting interests, *he can claim pay* for his services *from only one side* . . . ." (quoting 7 C.S.J. *Attorney and Client* § 167b (1955))); Eriks v. Denver, 824 P.2d 1207, 1213 (Wash. 1992) ("Where [an attorney] . . . was serving more than one master or was subject to conflicting interests, he should be denied compensation. It is no answer to say that fraud or unfairness were not shown to have resulted. . . ." (quoting Woods v. City Nat'l Bank & Tr. Co. of Chi., 312 U.S. 262, 268–69 (1941))).

428. *See* Moses v. McGarvey, 614 P.2d 1363, 1372 (Alaska 1980) (explaining an attorney who has breached his or her fiduciary duty by representing two or more clients with conflicting interests should receive no compensation as punishment); Jensen v. Bowen, 164 N.W. 4, 5 (N.D. 1917) (stressing the rule is based on public policy and is intended to be both remedial and preventative); Plotner v. Chillson & Chillson, 95 P. 775, 777 (Okla. 1908) ("A broker acting for both parties in effecting an exchange of property can recover compensation from neither, unless his double employment was known and assented to by both." (quoting Rice v. Wood, 113 Mass. 133, 133 (1873))); *see also* Strong v. Int'l Bldg., Loan & Inv. Union, 55 N.E. 675, 676 (Ill. 1899) (per curiam) (noting public policy demands an attorney not be entitled to the compensation for services rendered when he simultaneously represented parties in conflict).

429. *See* Garrick v. Weaver, 888 F.2d 687, 691–92 (10th Cir. 1989) (awarding quantum meruit to a lawyer because, despite some impropriety, the lawyer still performed valuable and beneficial legal services (citing Ross v. Scannell, 647 P.2d 1004, 1010–11 (Wash. 1982) (en banc))); Iannotti v. Mfrs. Hanover Tr. Co. (*In re* N.Y., New Haven & Hartford R.R. Co.), 567 F.2d 166, 175 (2d Cir. 1977) ("[R]ecognition of the general rule, however, does not strike us as a mandatory requirement that reorganization courts woodenly must deny compensation in every case of conflict of interest, regardless of the facts." (citing Woods v. City Nat'l Bank & Tr. Co. of Chi., 312 U.S. 262, 269 (1941))).

430. *See* Rodriguez v. Disner, 688 F.3d 645, 655 (9th Cir. 2012) ("We are not aware, however, of any California case that has overturned a trial court's decision to deny attorneys' fees to an attorney engaged in dual representation of clients with actual conflicts of interest . . . ."); Frank Settelmeyer & Sons, Inc. v. Smith & Harmer, Ltd., 197 P.3d 1051, 1059 n.33 (Nev. 2008) (agreeing it was an abuse of discretion to disqualify an attorney where no actual conflict existed; stating potential conflicts of interest are not sufficient (citing Bottoms v. Stapleton, 706 N.W.2d 411, 417 (Iowa 2005))).

concludes the lawyer's representation of a second client would significantly jeopardize the first client's confidential information.[431] If so, the injunction is issued to disqualify the lawyer.[432]

Just as the plaintiff is not required to prove damages, the benefits of the defendant's services are not generally considered relevant to the issue of liability or the possibility of apportionment,[433] except, apparently, when they are relevant.[434]

Disloyal Competition: The actions of a fiduciary competing with the principal (without the principal's knowledge and waiver) might be called disloyal competition.[435] There are two key issues to this form of disloyalty. The first relates to the timing of the specific actions. Most state

431. *See* Maritrans GP Inc. v. Pepper, Hamilton & Scheetz, 602 A.2d 1277, 1284 (Pa. 1992) ("While the breach by a lawyer of his duty to keep the confidences of his client and to avoid representing conflicting interests may be the subject of appropriate disciplinary action, a court is not bound to await such development before acting to restrain improper conduct where it is disclosed in a case pending in that court." (quoting Slater v. Rimar, Inc., 338 A.2d 584, 589 (Pa. 1975))).

432. *Id.* ("[A] court may restrain conduct which it feels may develop into a breach of ethics; it 'is not bound to sit back and wait for a probability to ripen into a certainty.'" (quoting United States v. RMI Co., 467 F. Supp. 915, 923 (W.D. Pa. 1979))).

433. United States *ex rel.* Rural Util. Serv. v. Schilling (*In re* Big Rivers Elec. Corp.), 355 F.3d 415, 437 (6th Cir. 2004) ("No doubt the sanction in this case is a harsh and unforgiving one. Schilling's efforts, he claims, brought approximately $145 million of new value into the estate. Rather than the thanks of a grateful court and the thanks of grateful parties, he received an order to reimburse the debtor nearly $1 million in fees. Steep as the sanction may be, it represents the price of disloyalty, a price the courts have not hesitated to charge in dealing with similar breaches of trust.").

434. *See* Allapattah Servs. v. Exxon Corp., 454 F. Supp. 2d 1185, 1238 (S.D. Fla. 2006) (holding the lawyer's fee splitting agreement did not warrant full forfeiture, reducing the fee incentive award by 25% and denying disproportionate incentive award because the lawyer was instrumental in the case). In *Zeisl v. Watman*, the Second Circuit found, despite the presence of conflicting interests, in light of the circumstances and actions by the attorneys demonstrating good faith, the attorney should not be required to forfeit their fees:

> There is not the slightest indication that any of the Class Counsel who were engaged in this enormously complicated undertaking acted with anything less than the utmost good faith. They achieved extraordinarily beneficial results for their clients. To whatever extent their representation of the Austrian Settlement Class placed them in a position of potential conflict, they have thus far not even applied to the District Court for any compensation for that representation. In sum, no basis exists for obliging counsel for the Austrian Settlement Class to forfeit the fees awarded to them by the German Foundation for their efforts, in cooperation with many other lawyers, to achieve an extraordinary extrajudicial remedy for victims of the Holocaust.

Zeisl v. Watman (*In re* Austrian & German Bank Holocaust Litig.), 317 F.3d 91, 105 (2d Cir. 2003).

435. *See infra* App. 1 (showing the remedies awarded for the following three disloyal competition cases: *HTS, Inc. v. Boley*, 954 F. Supp. 2d 927 (D. Ariz. 2013); *Vibra–Tech Engineers, Inc. v. Kavalek*, 849 F. Supp. 2d 462 (D.N.J. 2012); and *Dowd & Dowd, Ltd. v. Gleason*, 816 N.E.2d 754, 771 (Ill. App. Ct. 2004)).

courts have held employees are entitled to prepare to compete but cannot actually start to compete before they are off the payroll as long as the employee does not contact the employer's customers to arrange for them to change vendors.[436] *Eckard Brandes, Inc. v. Riley*[437] is notable because employees, using their employer's confidential information, bid on and secured a new contract while still employed for a company that competed for that same contract.[438] Recently, the Second Circuit had occasion to hold diverting business from one's employer to a competitor is the same as disloyal competition.[439]

The second issue relates to measuring damages or the employee's unjust enrichment. In some cases the employee's customers are distinguished between new customers and customers that had existing relationships with the employer.[440] The measure of damages for obtaining new customers

436. *E.g.*, Taser Int'l, Inc. v. Ward, 231 P.3d 921, 927 (Ariz. Ct. App. 2010) (finding no disloyal competition where a current employee began business plans and discussions with an attorney for a competing business).

437. Eckard Brandes, Inc. v. Riley, 338 F.3d 1082 (9th Cir. 2003).

438. *Id.* at 1085 ("Although an employee 'is entitled to make arrangements to compete' with his employer prior to terminating the employment relationship, the employee is not 'entitled to solicit customers for such rival business before the end of his employment.'" (quoting RESTATEMENT (SECOND) OF AGENCY § 399 cmt. e (AM. LAW INST. 1958))). Another glaring instance of employee disloyalty can be seen in *Wenzel v. Hopper & Galliher* where an employee was found in a fax communication to have clearly crossed over from preparation into competition by soliciting a customer for his subsequent employer prior to his resignation from the former. Wenzel v. Hopper & Galliher, PC, 830 N.E.2d 996, 1001 (Ind. Ct. App. 2005); *see also* Vigneau v. Storch Eng'rs, No. CV 890700122S, 1995 WL 767984, at *8–10 (Conn. Super. Ct. Dec. 4, 1995) (awarding, in a case that awarded substantial legal fees and punitive damages for another claim, compensatory damages for profits lost from the employee's competition against his employer for two projects but denying compensation forfeiture due to the isolated nature of the competition); Efird v. Clinic of Plastic & Reconstructive Surgery, PA, 147 S.W.3d 208, 220 (Tenn. Ct. App. 2003) (reversing a summary judgment in favor of the employee in light of the employee's actions, which went "well beyond mere preparation to open his own practice"); Prince, Yeates & Geldzahler v. Young, 94 P.3d 179, 184–86 (Utah 2004) (holding the law associate must disgorge the billings from the clients he billed while still in the employ of the claimant but denying compensation forfeiture).

439. Design Strategy, Inc. v. Davis, 469 F.3d 284, 300–302 (2d Cir. 2006) (holding the employee's salary should be forfeited for diverting potential business to his employer's competitor just as if the employee were competing with his employer); Demoulas v. Demoulas Super Market, Inc., 677 N.E.2d 159, 188 (Mass. 1997) (finding liability "even where the profits or benefits accrue to a third party, whether or not it is under the control of the [employee]"), *aff'd*, 703 N.E.2d 1141 (Mass. 1998). *But see* Johnson v. Brewer & Pritchard, PC, 73 S.W.3d 193, 203 (Tex. 2002) ("We hold only that an associate may participate in referring a client or potential client to a lawyer or firm other than his or her employer without violating a fiduciary duty to that employer as long as the associate receives no benefit, compensation, or other gain as a result of the referral.").

440. *E.g.*, Dental Health Prods., Inc. v. Ringo, No. 08-C-1039, 2011 WL 4585331, at *3, *5 (E.D. Wis. Sept. 30, 2011) (distinguishing between the current case where employees took business directly from the employer from a previous decision where employees diverted business that was not otherwise going to be given to the employer).

while still employed is the profits from those customers up until the termination of employment, but the measure of damages for converting the employer's established customers can continue after the employee leaves the employer.[441]

Some employment scholars have objected to the inclusion of all employees for this type of employee disloyalty, citing *Berry v. Goodyear Tire & Rubber Co.*[442] in which an hourly worker at a tire store was held to be disloyal by moonlighting for a competitor.[443] In that case, the defendant took paid medical leave (which was not substantiated by a doctor) and conducted business for a competitor of his employer.[444] The court did not address a claim for forfeiture, but it did confirm that the employee of nineteen years of service had been terminated for cause and was not entitled to normal termination benefits.[445]

This is an area of disloyalty in which other remedies in equity, such as injunction, rescission, and constructive trust, are more prevalent—which, in many cases, is due to difficulties in measuring actual damages or benefits[446] or the need to pursue an accounting.[447] Based only on

441. NCMIC Fin. Corp. v. Artino, 638 F. Supp. 2d 1042, 1084 (S.D. Iowa 2009) (applying Iowa law and stating, "When a disloyal employee breaches his fiduciary duty to his employer by diverting business to the employer's competitors, the employer can recover damages for diverted current business, diverted future business, and misappropriated assets."); *see also* V.I.M. Recyclers, LP v. Magner, No. 03 C 343, 2005 WL 1745657, at *20 (N.D. Ill. July 21, 2005) (forfeiting the compensation of an employee who diverted several company accounts to other competitors and awarding the wronged company lost profits for the period of the employee's disloyalty and the subsequent two years following the employee's termination); Vendo Co. v. Stoner, 321 N.E.2d 1, 13, 15 (Ill. 1974) (awarding $7,345,000 of total damages, including $2,135,000 of lost profits, $170,835 of compensation forfeiture, and $5,039,165 of lost value of the employer's enterprise).

442. Berry v. Goodyear Tire and Rubber Co., 242 S.E.2d 551 (S.C. 1978).

443. In *Berry*, a sales employee with nineteen years of service at a tire outlet took a paid medical leave of absence, during which he failed to substantiate his medical condition. *Id.* at 552. The employer eventually determined the employee was working for a competing tire outlet on the phone at his home. *Id.* The court found the employee's actions were disloyal. *Id.* at 553 (concluding the breach of duty "disqualified him from any right he may have had to 'release pay' compensation").

444. *Id.* at 552.

445. *Id.*

446. *See* Ennis v. Interstate Distribs., Inc., 598 S.W.2d 903, 906–07 (Tex. Civ. App.—Dallas 1980, no writ) (holding, despite the fact that damages could not be determined because the buyer could not reasonably measure damages, rescission for breach of contract was proper even though the service contract was partially fulfilled); *see also* Harry R. Defler Corp. v. Kleeman, 243 N.Y.S.2d 930, 937 (App. Div. 1963) (entitling the plaintiff to an injunction, permanently preventing the defendants from continuing to use the plaintiff's customers list, and finding an accounting of the defendants' profits may be insufficient to compensate plaintiff), *aff'd*, 225 N.E.2d 569 (N.Y. 1967).

447. *See* Mar. Fish Prods., Inc. v. World-Wide Fish Prods., Inc., 474 N.Y.S.2d 281, 287 (App. Div. 1984) ("Thus, an accounting is warranted to ascertain the damages resulting from Christensen's diversion of business during the entire fourteen-month period from December 1975, when he

personal experience, this is also an area in which companies are reluctant to explore and expose causation issues about existing or potential clients in public court, let alone to ask those clients to testify about why they chose one competitor over the other.

Self-dealing: The traditional case involves real estate agents or brokers who act for the principal to buy or sell property.[448] To self-deal, the disloyal fiduciary will hide the real seller or buyer, creating an intermediary "shill," and arrange for the principal to pay too much or sell for too little to the shill who then "flips" the property to make a profit from the transaction with the hidden seller or buyer.[449] As these actions also constitute failure to disclose important information, this would qualify as fraud or constructive fraud.[450] The standard remedy is for the court to disgorge the profit and the fee (almost always the entire fee without apportionment).[451] The profit derived from the disloyal transaction may be disgorged as either gross or net of necessary expenses to complete the transaction.[452]

incorporated World-Wide, until February 11, 1977, when he resigned from Maritime."); *see also* Chernow v. Reyes, 570 A.2d 1282, 1285 (N.J. Super. Ct. App. Div. 1990) ("Defendant and his corporation are liable for any profits earned in a competitive business while he was employed by plaintiff. . . . The agent holds such profits in a constructive trust for the principal.").

448. *See, e.g.*, Ellison v. Alley, 842 S.W.2d 605, 606 (Tenn. 1992) (concluding a breach of fiduciary duty existed when the real estate brokers received nearly half of the total purchase price of the property through misrepresentation to both buyer and seller because of the broker's undisclosed possession of an option to purchase at a much lower price).

449. In *Ellison*, the court found the real estate brokers, a father and son team working together in conspiracy, acted in bad faith and were, consequently, not entitled to reasonable fees for their services:

> We are in agreement with the finding of breach of fiduciary duty and the award to the plaintiff of the defendant's profits. But, on the narrow issue upon which this appeal was granted, we find that the defendants are not entitled to a commission on the sale of the Ellison property. It is apparent that the defendants manipulated both the Myers and Ellison transactions in such a manner as to willfully, and wrongfully, conceal their true role and their intention to reap a $180,000 ill-gained profit from the sale of the property.

Id. at 607–08; *see also* Collins v. McClurg, 29 P. 299, 301–02 (Colo. App. 1892) (finding a breach of the principal–agent relationship where real estate broker received $2,000 more from purchasers of property than the broker disclosed to the seller).

450. *See* Sutherland v. Guthrie, 103 S.E. 298, 301 (W. Va. 1920) ("Upon discovery of this fraud, it was held that he would have to account for the money so advanced in excess of the amounts actually paid for property purchased, and also that because of his conduct in this regard he would not be entitled to receive the [5%] commissions stipulated to be paid him for his services." (citing Shaeffer v. Blair, 149 U.S. 248, 256–57 (1893))).

451. *See* Shaeffer v. Blair, 149 U.S. 248, 256–57 (1893) (ordering the fraudulent agent to disgorge profits under the contract, commission fees, and net profits).

452. *See, e.g.*, Anderson Cotton Mills v. Royal Mfg. Co., 20 S.E.2d 818, 823–25 (N.C. 1942) (holding the measure of the fiduciary's profits should allow deductions for cleaning and thereby

Secret Profit: A secret profit is generally any undisclosed profit or benefit for the fiduciary.[453] It includes but is not limited to bribes.[454] But for accepted business practice, the frequent flyer miles obtained for employer travel could also be included in this category.[455]

Duty to Disclose: The duty to disclose is complicated only because it overlaps with all of the other forms of disloyalty—e.g., if the agent accrues a secret profit, she has a duty to disclose and disgorge the profit.[456] This

improving the value of the cotton waste at issue).

453. *See* Tomsic v. Lautieri (*In re* Tri–Star Techs. Co.), 257 B.R. 629, 636 (Bankr. D. Mass. 2001) ("It is well settled that an employer can recover from an employee any secret profit or benefit received as a result of business activities in conflict with the employee's duties to the employer."); *see also* Arst v. Stifel, Nicolaus & Co., 954 F. Supp. 1483, 1491 (D. Kan. 1997) (reviewing *Burton Enterprises, Inc. v. Wheeler*, which awarded both secret profit and compensation forfeiture, and explaining, because of the "'high standard' of loyalty established by Kansas courts, the faithless servant doctrine would not be limited to 'the blatant misappropriation of funds'" (quoting Burton Enters., Inc. v. Wheeler, 643 F. Supp. 588, 591 (D. Kan. 1986))); Tarnowski v. Resop, 51 N.W.2d 801, 802 (Minn. 1952) (stating "all profits made by an agent in the course of an agency belong to the principal, whether they are the fruits of performance or the violation of an agent's duty, is firmly established and universally recognized"); Rodgers v. Lenox Hill Hosp., 657 N.Y.S.2d 616, 621 (App. Div. 1997) ("[A]n employee who makes a profit or receives a benefit in connection with transactions conducted by him on behalf of his employer is under a duty to give such profit or benefit to his employer, whether or not it was received by the employee in violation of his duty of loyalty." (citing RESTATEMENT (SECOND) OF AGENCY §§ 388, 403 (AM. LAW INST. 1958))); *Sutherland*, 103 S.E. at 299 (recognizing "if the sale . . . had been consummated, and the plaintiffs had secured . . . secret profits in addition to the compensation provided in their contract, they would not be allowed to retain the same[] but would have to account to their principal for it").

454. *See* Williams Elecs. Games, Inc. v. Garrity, 366 F.3d 569, 576 (7th Cir. 2004) ("The victim of commercial bribery, . . . can obtain . . . either the damages that he has sustained . . . or the profits that the bribe yielded . . . . The total profits would consist of the bribe . . . plus the revenue . . . generated for the briber, minus the cost of goods sold and any other variable costs incurred in making the sales . . . ." (citation omitted)); *see also* 2 DOBBS, *supra* note 6, § 10.6, at 700 ("[T]he cases allow recovery of the bribe amount from the briber either as restitution or as damages." (footnote omitted)).

455. *See* Blake Fleetwood, *Frequent-Flyer Programs Are Convoluted, Mysterious, and a Maddening Fraud*, HUFFINGTON POST (May 4, 2011, 6:54 PM), http://huffingtonpost.com/blake-fleetwood/frequentflier-programs-ar_b_856623.html (pointing out, while frequent flyer programs are commercial bribery, people are not charged with the crime because of the millions of people taking part).

456. The Indiana Supreme Court comments on this issue in *Nichols v. Minnick*:

> Although we agree that there is no proof of loss to support tort damages, we do not agree with the trial court's conclusion that disgorgement is not required. The trial court based its judgment on its finding that Nichols had reason to know of the relationship between Minnick and Blickensdorf, and its conclusion that Minnick's failure to disclose the $15,000 loan for the down payment "was not a serious violation of a duty of loyalty or seriously disobedient conduct such that Minnick should be ordered to repay the commission he received to Nichols." . . . [A] fiduciary is required to disgorge any benefit from failure to disclose material information. The trial court's conclusion is inconsistent with its findings of breach of fiduciary duty and materiality.

is particularly important in cases where the principal claims legal malpractice and breach of fiduciary duty, arguing the breach of the agent's duty is legal malpractice and the failure to disclose that breach is a breach of fiduciary duty.[457]

In *Grassgreen*, the breach of the duty to disclose was applied to extend the disloyalty period beyond the time interval in which the defendants committed the disloyal transactions.[458] Under that approach, the disloyalty period would be the time in between the act of disloyalty and the date the principal finally found out about that disloyalty.[459]

Confidentiality: Almost 100 years ago, when the concept of property rights in trade secrets was new and controversial, Justice Holmes stated that, while the property rights issue might be in doubt, the betrayal of the malefactor's relationship with his employer was not, and that disloyalty should be the basis for the claim.[460] This is an area in which courts are sometimes inclined to issue injunctive relief to remove the defendant's temptation to breach her principal's confidentiality. For example, the Pennsylvania court upheld an injunction to disqualify a lawyer from representing a former client's competitor even though no evidence was introduced that the lawyer had actually breached the former client's

Nichols v. Minnick, 885 N.E.2d 1, 5 (Ind. 2008); *see also* Boston Children's Heart Found., Inc. v. Nadal-Ginard, 73 F.3d 429, 434 (1st Cir. 1996) (affirming an award of forfeiture of three years of compensation and benefits because the defendant set his own salary but failed to inform his board of directors that he was employed and compensated significantly by another medical institution).

457. *See, e.g.*, Gibson v. Ellis, 126 S.W.3d 324, 330 (Tex. App.—Dallas 2004, no pet.) ("[T]he evidence did not conclusively establish the omissions were made for the purposes of achieving an improper benefit from Ellis's representation of Gibson.").

458. Enstar Grp., Inc. v. Grassgreen, 812 F. Supp. 1562, 1583 (M.D. Ala. 1993).

459. *Id.* at 1566 (extending the duty for the time and money spent on investigating whether improper benefits had been received).

460. Specifically, Justice Holmes stated:

> Whether the plaintiffs have any valuable secret or not the defendant knows the facts, whatever they are, through a special confidence that he accepted. The property may be denied but the confidence cannot be. Therefore the starting point for the present matter is not property or due process of law, but that the defendant stood in confidential relations with the plaintiffs, or one of them. These have given place to hostility, and the first thing to be made sure of is that the defendant shall not fraudulently abuse the trust reposed in him.

E.I. Du Pont De Nemours Powder Co. v. Masland, 244 U.S. 100, 102 (1917); *see also* Oberly v. Kirby, 592 A.2d 445, 463 (Del. 1991) (indicating unjust enrichment results when a fiduciary garners a profit by using information it obtained through a confidential relationship, "even if such profit or advantage is not gained at the expense of the fiduciary" and such enrichment "will not be countenanced by a Court of Equity"); Diamond v. Oreamuno, 248 N.E.2d 910, 912 (N.Y. 1969) ("The primary concern, in a case such as this, is not to determine whether the corporation has been damaged but to decide, as between the corporation and the defendants, who has a higher claim to the proceeds derived from the exploitation of the information.").

confidentiality.[461]

In the case appropriately styled *Sealed Party v. Sealed Party*,[462] the court found a lawyer's breach of client confidentiality had apparently failed the test for sufficient egregiousness to award forfeiture.[463] The client was in a delicate dispute with a customer and went to lengths to ensure confidentiality in hopes of minimizing embarrassment and disruption to the relationship. The successful settlement of the dispute included a specific confidentiality agreement between the parties and their attorneys. However, a law partner, who was only tangentially involved in the actual litigation, made a press release touting the firm's success and naming the parties.[464] The judge's opinion is noteworthy because it held that finding the lawyer liable for breach of fiduciary duty was a sufficient remedy without forfeiture.[465] This decision demonstrates the changes introduced by the Restatement (Third) of the Law Governing Lawyers, which reverses the tradition of shifting burdens of proof into a process of assigning burdens exclusively to the plaintiff,[466] and introduces the condition that the breach be "clear and serious," which in this case, appears to be lost in

461. Maritrans GP Inc. v. Pepper, Hamilton & Scheetz, 602 A.2d 1277, 1286–87 (Pa. 1992) (concluding "the danger of revelation of the confidences of a former client [was] so great that injunctive relief [was] warranted"). The court notes a lesser injunction "might be theoretically possible[,] . . . but such an injunction would be difficult, if not impossible, to administer." *Id.* at 1284 ("[A] court may restrain conduct which it feels may develop into a breach of ethics; it 'is not bound to sit back and wait for a probability to ripen into a certainty.'" (quoting United States v. RMI Co., 467 F. Supp. 915, 923 (W.D. Pa. 1979))); *see also* Henderson v. Rep Tech, Inc., 557 N.Y.S.2d 224, 225 (App. Div. 1990) ("[T]he remedies of forfeiture, a permanent injunction, and the dismissal of plaintiff's claims [was] proper. . . . The compensation paid an employee during the period of disloyalty is a component of the profit for which an employee must account and is subject to forfeiture.").

462. Sealed Party v. Sealed Party, No. Civ.A. H-04-2229, 2006 WL 1207732 (S.D. Tex. 2006).

463. *Id.* at *20.

464. *Id.* at *3.

465. *Id.* at *21.

466. The court notes:

> [T]he [c]lient has proven by a preponderance of the evidence that the [a]ttorney had a continuing fiduciary duty not to reveal confidential information to others, and that the [a]ttorney violated that duty by issuing the [p]ress [r]elease. The [c]lient, however, has not proven he suffered actual damages, if he even preserved the right to claim the damages he now seeks in this case. Nor has the [c]lient proven that the [a]ttorney benefitted financially or otherwise from the breach of fiduciary duty. The Court also concludes no fee forfeiture is warranted because the Court cannot conclude as to any single component of the [p]ress [r]elease that the [a]ttorney's breach of fiduciary duty was both clear and serious. The [c]lient therefore has failed to establish all the elements of a breach of fiduciary duty claim against the [a]ttorney under Texas law.

Id.

abstraction.[467] However, *Sealed Party* does confirm the principle that the duty of confidentiality extends beyond the actual attorney–client relationship.[468]

Billing Practices: The courts of some states differ on how to deal with claims relating to professional billing practices or expense reimbursement fraud.[469] Presumably the difference is one of degree—i.e., the minimum amount required for the court to hold the billing or expense practice as sufficiently fraudulent to constitute disloyalty. For example, in *Gemini Networks v. Nofs*,[470] the court may have been less predisposed to find

467. *See id.* at *20 (using its discretion, the court found there was a breach of duty but refused to order any forfeiture because the breach was not both clear and serious).

468. *See* Lerner Corp. v. Three Winthrop Props., Inc., 723 A.2d 560, 566 (Md. 1999) ("Unless otherwise agreed, after the termination of the agency, the agent: . . . . (d) has a duty to the principal not to take advantage of a still subsisting confidential relation created during the prior agency relation." (quoting RESTATEMENT (SECOND) OF AGENCY § 396 (AM. LAW INST. 1958))); Graham Mortg. Corp. v. Hall, 307 S.W.3d 472, 479 (Tex. App.—Dallas 2010, no pet.) (holding, although the party did not owe a fiduciary duty to defendant, he nevertheless breached his fiduciary duty by knowingly participating in the fiduciary's breach). Fiduciary duties generally terminate at the end of an employment relationship, but an "agent has a duty after the termination of the agency not to use or to disclose to third persons . . . trade secrets . . . or other similar confidential matters." NCH Corp. v. Broyles, 749 F.2d 247, 254 (5th Cir. 1985) (2nd & 3rd alterations in original) (quoting Standard Brands, Inc. v. Zumpe, 264 F. Supp. 254, 262 (E.D. La. 1967)).

469. In a case where an attorney overcharged his client by several hundred thousand dollars and received payment by making unauthorized withdrawals of over $900,000 from a trustee account, the court held the attorney was not required to disgorge his entire fee because, under New York law, attorneys "may be entitled to recover for their services, even if they have breached their fiduciary obligations." Mar Oil, SA v. Morrissey, 982 F.2d 830, 840 (2d Cir. 1993); *see also* Newman v. Silver, 553 F. Supp. 485, 496 (S.D.N.Y. 1982) (holding an attorney who unconscionably overcharged his client, thereby breaching his fiduciary duty, is, nevertheless, entitled to the fair value of services rendered), *aff'd in part*, *vacated on other grounds*, 713 F.2d 14 (2d Cir. 1983); Gemini Networks, Inc. v. Nofs, No. CV030824652, 2004 WL 113622, at *2 (Conn. Super. Ct. Jan. 8, 2004) (holding "inaccurate requests for reimbursement for expenses were the result of miscommunication"; thus, the fiduciary's actions were not fraud because he "was not 'radically unfaithful to his trust or guilty of gross misconduct'" (quoting Phx. Mut. Life Ins. Co. v. Holloway, 51 Conn. 310, 314 (1883))); *Lerner*, 723 A.2d at 567 (stating excess billing in another case does not trigger compensation forfeiture (citing Fairfax Sav., F.S.B. v. Weinberg & Green, 685 A.2d 1189, 1208–09 (1996))). *But see* Nimkoff Rosenfeld & Schecter, LLP v. RKO Props., Ltd., No. 07 Civ. 7983(DAB), 2011 WL 832859, at *3 (S.D.N.Y. Mar. 4, 2011) ("[A]llegations that [the fiduciary] engaged in verbal abuse and physical threats, charged an excessive fee, breached confidences, and asserted a lien on client funds to which they were not entitled, sound in breach of fiduciary duty." (citation omitted)); Riverwalk CY Hotel Partners, Ltd. v. Akin Gump Strauss Hauer & Feld, LLP, 391 S.W.3d 229, 239 (Tex. App.—San Antonio 2012, no pet.) (holding the client was entitled to file a separate breach of duty claim for unfair billing practices); Sullivan v. Bickel & Brewer, 943 S.W.2d 477, 483 (Tex. App.—Dallas 1995, writ denied) (affirming the plaintiff properly alleged a claim for fraudulent billing practices that was separate from the legal malpractice claim, which was otherwise denied for limitations).

470. Gemini Networks, Inc. v. Nofs, No. CV030824652, 2004 WL 113622 (Conn. Super. Ct. Jan. 8, 2004).

disloyalty in light of the disparity of the forfeiture sought ($654,635) and the amount overbilled ($31,861).[471]

E. *Compensation*

Compensation held forfeit may include wages, bonuses, retirement benefits, and grants of stock or stock options.[472] If the court also grants the claimant a constructive trust, forfeiture of stock or stock options would allow the claimant to trace the proceeds of the stock or stock options that have been sold or exercised and reinvested to another investment that has appreciated.[473]

In a couple of cases, courts have considered defendants' expense reimbursements, such as leasehold improvements to their office, elaborate parties, or trips, as compensation.[474] To distinguish between appropriate expenses and disguised forms of compensation, a court will usually apply a test borrowed from trust law, which evaluates whether the expenditure benefited the principal.[475]

One of the unusual forms of compensation forfeiture occurred in *Phansalkar v. Andersen Weinroth & Co.*,[476] in which the defendant was an executive at a private merchant bank.[477] As a part of his compensation,

471. *Id.* at *1–2 (concluding the defendant's testimony that overbilling was a miscommunication between attorney and secretary was credible).

472. *See* Enstar Grp., Inc. v. Grassgreen, 812 F. Supp. 1562, 1575 (M.D. Ala. 1993) (holding the defendant should "forfeit all salary, bonuses, and other compensation which were paid to him by his corporation while he was in breach of his duties").

473. The claimant would have the option to accept the ex ante value of the stock or stock options on the date of the breach or its value as of the date of trial. *See id.* ("A trustee is not allowed to offset losses against gains in regard to his liability for breaching his trust.").

474. *See* Heyman v. Kline, 344 F. Supp. 1110, 1115 (D. Conn. 1970) (stating the compensation to be forfeited is broadly defined to include money paid to or spent directly for the employee's benefit, including personal expenses reimbursed by the employer), *rev'd on other grounds*, 456 F.2d 123 (2d Cir. 1972); Dowd & Dowd, Ltd. v. Gleason, 816 N.E.2d 754, 771 (Ill. App. Ct. 2004) (noting, while the court ordered forfeiture for some expense account items, it did not include the costs of the trip to Bermuda or the Allstate lawyers' section Christmas party because "there is no way to determine whether or not the GMS firm benefitted from those matters, or if Plaintiff would have had them in any event, even if it had known that Gleason was leaving").

475. *See Gleason*, 816 N.E.2d at 771 (discussing the defendant's breach of fiduciary duty, which occurred when he acted for his own benefit, disregarding the interest of his prior firm).

476. Phansalkar v. Andersen Weinroth & Co., 344 F.3d 184 (2d Cir. 2003) (per curiam).

477. The court's description of the facts of this case was that the fiduciary

> acted in a manner inconsistent with his agency by withholding from AW cash, stocks, and other interests that belonged to AW and that should have been turned over to the firm, as a part of the firm's only reliable source of income. He also acted in a manner inconsistent with his agency by specifically declining Sync's offer to place an AW designee on its board, without having told AW of the opportunity. In addition, he repeatedly violated his affirmative duty to

the executive was offered opportunities to invest on the same terms as the firm.[478] But because he failed to disclose six distinct instances of secret profit, the firm fired him and denied him the stock he had previously elected to purchase, which had greatly appreciated to a profit of more than $4 million.[479] Upon appeal to the Second Circuit, the firm was awarded specific restitution of that stock (a remedy in equity), just as Enstar was granted specific restitution of Grassgreen's holdings in MacPherson.[480] Thus, in general, remedies in equity can be very effective for plaintiffs who seek the return of assets that have appreciated in value between the date of the tort and the date of the trial.[481]

Forfeiture is an unusual form of a remedy in equity because it does not allow for counter-restitution or offsets for necessary expenses or revenue passed through to another party. For example, if a principal sued a business operation for breach of fiduciary duty and disloyalty and sought the remedy of disgorgement, the defendant's enrichment would be measured as profit, not gross fees; the defendant's fiduciary business would normally be allowed to offset its revenue with expenditures that benefited the principal, which might include payroll for support staff and out-of-pocket expenses.[482] However, it is still likely the salary of the particular fiduciary would not be deductible as an "infringing expense."[483]

There is a long history behind allowing counter-restitution, which relates back to the traditions in equity, out of concern for the total equity of its orders and holdings.[484] Thus, it is just as important to the law in equity that neither party to a suit be unjustly enriched—i.e., no order for a remedy in equity should unjustly enrich the plaintiff. In *Scrushy v.*

give AW the Directors' Compensation he received on AW's behalf. These breaches are more than sufficient to warrant forfeiture.

Id. at 203–04.

478. *See id.* at 193–95 (discussing three investment opportunities offered to the executive, which he thought to be 'good deals').

479. *Id.* at 197–98.

480. *Id.* at 210; Enstar Group, Inc. v. Grassgreen, 812 F. Supp. 1562, 1576 (M.D. Ala. 1993).

481. *See* Laycock, *supra* note 8, at 1284 ("The restitutionary claim matters . . . when plaintiff prefers specific restitution . . . because the thing plaintiff lost has changed in value . . . .").

482. *See* Roach, *supra* note 78, at 1291–97 (noting unjust enrichment may generally offset reasonable expenditures that benefit the plaintiff).

483. *See* Roach, *supra* note 401, at 520–22 (discussing the Restatement (Third) of Restitution and Unjust Enrichment, which allows defendants' expenses and expenditures to be rejected as infringing expenses).

484. *See* Rounds, Jr., *supra* note 374, at 349 (explaining the "equitable right of indemnity is grounded in Equity's contribution to the law of unjust enrichment, specifically the equitable right of counter-restitution").

Tucker,[485] Richard Scrushy raised this issue and asserted it was inequitable for the trial court to award forfeiture of his gross income rather than income net of all applicable taxes.[486] The Alabama Supreme Court's response was unsympathetic.[487]

The absence of counter-restitution, however, raises the real specter of a disproportionately punitive remedy because the defendant is forced to disgorge a sum greater than her profit or gain. As the U.S. Supreme Court said in *Snepp v. United States*,[488] disgorgement of profit cannot be disproportionately punitive because the remedy is limited to profit.[489] Despite disagreement previously on issue, the modern trend seems to deny income taxes as an offset against the defendant's gross income when measuring unjust enrichment.[490]

F. *Apportionment*

Assuming the fiduciary or employee has been proven to have engaged in at least some disloyalty, the next most significant issue is how the identified compensation should be included between forfeiture for disloyalty or excluded as not "tainted by the disloyal acts." According to the Restatement (Second) of Agency, apportionment starts with the retainer agreement or employment contract.[491] If the agreement provides for payment by time period or by task, then any apportionment must be consistent with the contract.[492] So, if the employee is a salesman and is

485. Scrushy v. Tucker (*Scrushy I*), 955 So. 2d 988 (Ala. 2006).

486. *Id.* at 1012.

487. *See id.* (finding no merit to Scrushy's argument since he "was credited with the gross amount, and HealthSouth was concomitantly deprived of the amount paid to Scrushy in bonuses, regardless of whether Scrushy paid a certain percentage of those funds in taxes[,]" and stating "[w]hether Scrushy can obtain a refund of the taxes paid upon his restitution of the bonuses is a matter between Scrushy and the taxing authorities"). For more context on Richard Scrushy, see discussion *infra* Section V.A.

488. Snepp v. United States, 444 U.S. 507 (1980) (per curiam).

489. *See id.* at 515–16 (explaining constructive trust remedies "[conform] relief to the dimensions of the wrong" and noting, "since the remedy reaches only funds attributable to the breach, it cannot saddle the former agent with exemplary damages out of all proportion to [the] gain").

490. Nike Inc. v. Wal-Mart Stores, 138 F.3d 1437, 1448 (Fed. Cir. 1998) (citing Schnadig Corp. v. Gaines Mfg. Co., 620 F.2d 1166, 1169–71 (6th Cir. 1980)). Perhaps owing to the fact that the plaintiff in *Snepp* was the U.S. government, Frank Snepp, a defendant, was allowed to offset income taxes paid in the measure of disgorgement. *See* FRANK SNEPP, IRREPARABLE HARM 357 (Univ. Kan. Press 1999) (recounting that the district court did, however, allow Snepp to offset his income taxes).

491. *See* RESTATEMENT (SECOND) OF AGENCY § 399 (AM. LAW INST. 1958) (providing an appropriate remedy for the agent's breach might be "an action on the contract of service").

492. *See* G.K. Alan Assoc., Inc. v. Lazzari, 840 N.Y.S.2d 378, 386 (App. Div. 2007) (noting "the principal is obligated to pay to the agent, despite the breach . . . 'for services properly rendered'" and,

paid by commission, he will need to forfeit commissions only on accounts or sales that were tainted by the disloyalty.[493] Since the predominant agreement is to pay by the week, fortnight, or month, most forfeiture is undertaken by time period and begins accruing only after the first act of disloyalty.[494]

Similarly, some cases distinguish between different sources of the employee's compensation. In *Design Strategy, Inc. v. Davis*,[495] the Second Circuit affirmed the district court's decision to forfeit the employee's salary but not the employee's commissions, which were untainted by disloyalty.[496] In *Bank of Tokyo–Mitsubishi, Ltd. v. Malhotra*,[497] a bank sought nine years of forfeiture against an employee convicted of embezzlement, but its award was limited to forfeiture of the employee's

"[u]nder the Restatement view, . . . 'the agent is entitled to retain compensation only for properly performed tasks for which compensation is specifically apportioned by contract'" (citations omitted) (first quoting AGENCY § 456; and then quoting Interpool Ltd. v. Patterson, 874 F. Supp. 616, 621 (S.D.N.Y. 1995))), *aff'd*, 893 N.E.2d 133 (N.Y. 2008); *see also* Heyman v. Kline, 344 F. Supp. 1110, 1115 (D. Conn. 1970) ("[T]he plaintiffs should recover all compensation given to defendant within the terms of the various employment contracts."), *rev'd on other grounds*, 456 F.2d 123 (2d Cir. 1972); Hartford Elevator, Inc. v. Lauer, 289 N.W.2d 280, 286 (Wis. 1980) ("If an agent is paid a salary apportioned to periods of time, . . . he is entitled to receive the stipulated compensation for periods or items properly completed before his renunciation or discharge." (quoting AGENCY § 456 cmt. b)).

493. *See* Nat'l Legal Research Grp., Inc. v. Lathan, 42 F.3d 1386, Nos. 93-1844, 93-1884, 1994 WL 667058, at *3 (4th Cir. Nov. 30, 1994) (per curiam) (unpublished table decision) ("The district court's decision allows [the agent] to retain only commissions he received for customer sales that were not tainted by his disloyalty and that benefitted [the principal].").

494. *See* Phansalkar v. Andersen Weinroth & Co., 344 F.3d 184, 188 (2d Cir. 2003) (per curiam) (adhering to New York's faithless servant doctrine and holding the plaintiff is required "to forfeit all compensation received after his first disloyal act" since "there was no agreement for [the plaintiff's] compensation to be determined on a task-by-task basis"); Musico v. Champion Credit Corp., 764 F.2d 102, 113 (2d Cir. 1985) (noting a trend in recent cases that take a position that "calls for apportioning forfeitures when an agent's compensation is allocated to periods of time or to the completion of specified items of work"). For an interesting exception concerning forfeited compensation that was paid before the period of disloyalty, see *Dowd & Dowd, Ltd. v. Gleason*, which notes:

> Although the bonuses were based in part on work performed antecedent to the period of breach (established here as beginning on August 7, 1990), they were properly included in the damages award in that the departing partners had already contemplated and discussed leaving the firm by the time the bonuses were voted upon. Nonetheless, they did not notify the firm of their intentions until after both bonuses had been issued. Because the bonuses issued here appear to be based on both past performance and as an inducement to perform well in the future, we cannot say that it was an abuse of discretion for defendants to have to forfeit those amounts.

Dowd & Dowd, Ltd v. Gleason, 816 N.E.2d 754, 772 (Ill. App. Ct. 2004).

495. Design Strategy, Inc. v. Davis, 469 F.3d 284 (2d Cir. 2006).

496. *Id.* at 301–02.

497. Bank of Tokyo–Mitsubishi, Ltd. v. Malhotra, 131 F. Supp. 2d 959 (N.D. Ill. 2000).

bonuses.[498]

Apportionment policy is rarely absolute and defies precise characterization. However, three state opinions have been found that suggest a firm policy on apportionment. Two of those opinions reversed a trial court for failing to award full forfeiture over a substantial period.[499] By that standard, New York's and Indiana's policies can be characterized as expecting full forfeiture in the absence of unusual circumstances. In contrast, the Idaho Supreme Court remanded a trial opinion in which the judge stated he had to award full forfeiture and showed no consideration of what the supreme court deems relevant or important factors.[500] Thus, Idaho could be classified as a state in which the trial courts have to consider apportionment and justify their conclusion based on a number of factors. These three states might be said to have established a continuum of flexibility for assessing apportionment.

Based upon issued opinions, one could expect Kansas,[501] Ohio[502] and

498. *See id.* at 962 (holding it would be uncalled for to make the defendant forfeit the entirety of his compensation).

499. *See* Nichols v. Minnick, 885 N.E.2d 1, 5 (Ind. 2008) ("[W]e do not agree with the trial court's conclusion that disgorgement is not required. . . . [Its] conclusion is inconsistent with its finding of breach of fiduciary duty . . . ."); *Bildman III*, 914 N.E.2d 36, 47 (Mass. 2009) ("The court held that where 'defendants engaged in repeated acts of disloyalty, complete and permanent forfeiture of compensation, deferred or otherwise, is warranted under the faithless servant doctrine.'" (quoting William Floyd Union Free Sch. Dist. v. Wright, 877 N.Y.S.2d 395, 397 (App. Div. 2009))).

500. *See* Rockefeller v. Grabow, 39 P.3d 577, 583–84 (Idaho 2001) (holding, in Idaho, compensation forfeiture is a flexible rule and remanding because the trial judge indicated no consideration of the factors relevant to possible apportionment), *aff'd*, 82 P.3d 450 (Idaho 2003).

501. In *Bessman v. Bessman*, the Kansas Supreme Court took an approach similar to New York's:

> [A] minor breach of duty, affecting only a single transaction, will not result in loss of compensation attributable and "apportioned" to other transactions properly carried out. On a temporal basis, a defalcation in one month will not necessarily cause a forfeiture of compensation for other months when services are performed in an unexceptionable manner. This is the concept denoted by the New York rule that the faithlessness must "permeate" the service to cause a *total* loss of compensation, and of the restaters' criteria for exercising judicial discretion in allowing or denying compensation to a trustee.

Bessman v. Bessman, 520 P.2d 1210, 1219–20 (Kan. 1974); *see also* Wellwin Drilling Corp. v. Rush, 963 P.2d 448, Nos. 77, 981, 78, 627, 1998 Kan. App. Unpub. LEXIS 524, at *17–18 (Kan. Ct. App. Sept. 4, 1998) (unpublished table decision) (determining, due to a lack of details regarding the plaintiff's "operations, it is impossible to tell, as a matter of law, whether [the agent's] unfaithfulness permeated his entire employment" and noting "the trier of fact must ascertain what compensation [the agent] should be required to forfeit as a result of his breach of fiduciary duties").

502. *See* Buckingham, Doolittle & Burroughs, LLP v. Bonasera, 157 Ohio Misc.2d 1, 2010-Ohio-1677, 926 N.E.2d 375, ¶ 56 (C.P.) ("Illinois has applied the rule that 'permits a complete forfeiture of any salary paid by a corporation to its fiduciary during a time when the fiduciary was breaching his duty to the corporation.' Indiana and New York have applied similar rules in departing-lawyer cases as well." (citation omitted) (quoting Dowd & Dowd, Ltd. v. Gleeson,

Alabama.[503] to take a similar approach to that taken in Indiana and New York. States such as Idaho and Texas rely on the Restatement (Third) of the Law Governing Lawyers, which lists specific factors to be considered for forfeiture.[504] Wisconsin and Massachusetts provide the fiduciary the opportunity to prove offsets to forfeiture based on proving the value of the fiduciary's services.[505] In some of the Wisconsin and Massachusetts cases, apportionment hinges on whether the employee spent a normal

816 N.E.2d 754, 771 (Ill. App. Ct. 2004))); *see also* Roberto v. Brown Cty. Gen. Hosp., 571 N.E.2d 467, 469 (Ohio Ct. App. 1989) (adopting the faithless servant doctrine articulated by the Kansas Supreme Court, which mandates an agent can have compensation denied for the period of disloyalty and requires disloyalty permeate the entire scope of an agent's service to qualify for complete compensation forfeiture).

503. *See* Shaffer v. Regions Fin. Corp., 29 So. 3d 872, 883–84 (Ala. 2009) (per curiam) (proclaiming Alabama follows the faithless servant doctrine as laid out in the Restatement (Second) of Agency, which provides an agent is not entitled to any compensation "for conduct which is disobedient or which is a breach of his duty of loyalty; if such conduct constitutes a wil[l]ful and deliberate breach of his contract of service, he is not entitled to compensation even for properly performed services for which no compensation is apportioned" (emphasis omitted) (quoting Edwards v. Allied Home Mortg. Capital Corp., 962 So. 2d 194, 209 (Ala. 2007))).

504. *See* Dernick Res., Inc. v. Wilstein, No. 01-13-00853-CV, 2015 WL 3981772 at *10 (Tex. App.—Houston [1st Dist.] June 30, 2015, no pet.) (noting the remedy of forfeiture depends on the circumstances to harbor the ultimate objective of protecting trust relationships and, therefore, the trial court should consider the availability of the other remedies and factors). The court lists several factors:

> the gravity and timing of the breach, the level of intent or fault, whether the principal received any benefit from the fiduciary despite the breach, the centrality of the breach to the scope of the fiduciary relationship, any other threatened or actual harm to the principal, the adequacy of other remedies, and whether forfeiture "fit[s] the circumstances and work[s] to serve the ultimate goal of protecting relationships of trust."

Id. (alteration in original) (quoting *Swinnea II*, 318 S.W.3d 867, 875 (Tex. 2010)); *see also* Rockefeller v. Grabow, 39 P.3d 577, 582 (Idaho 2001) (stressing the Texas Supreme Court rejected an automatic full forfeiture of compensation in favor of factors similar to those outlined in the Restatement (Second) of Agency). The court emphasizes, "[T]o require an agent to forfeit all compensation for every breach of fiduciary duty, or even every serious breach, would deprive the remedy of its equitable nature." *Id.* (quoting Burrow v. Arce, 997 S.W.2d 229, 241 (Tex. 1999)), *aff'd*, 82 P.3d 450 (Idaho 2003).

505. *See* Meehan v. Shaughnessy, 535 N.E.2d 1255, 1266–67 (Mass. 1989) (concluding, because the value of the attorneys' work was equal to the compensation received, there is no entitlement to full forfeiture since "a fiduciary may be required 'to repay only that portion of his compensation, if any, that was in excess of the worth of his services to his employer'" (quoting Chelsea Indus., Inc. v. Gaffney, 449 N.E.2d 320 (Mass. 1983))); Town Planning & Eng'g Assocs., Inc. v. Amesbury Specialty Co., 342 N.E.2d 706, 711 (Mass. 1976) (affirming all circumstances should be considered when evaluating whether compensation should be forfeited); Hartford Elevator, Inc. v. Lauer, 289 N.W.2d 280, 287 (Wis. 1980) ("We conclude that whether the agent should be denied all or any part of his compensation during the period in which he breached his duty of loyalty depends on consideration and evaluation of the relevant circumstances . . . .").

amount of time and effort on the job producing for the company.[506] Alternatively, the courts have effectively shifted the burden to the employer, holding forfeiture is not warranted unless the employer can prove the employee's value differed from the compensation.[507]

The policy of the courts in Illinois is one of the most difficult to characterize. Illinois courts, especially its supreme court, have issued a number of forceful opinions on compensation forfeiture, which suggests they have a policy similar to that of Indiana or New York.[508] However, such an inference is contradicted by *In re Marriage of Pagano*,[509] which emphasizes the need for Illinois courts to be flexible in apportionment judgments.[510] *Pagano* is one of two or three Illinois opinions that denied any forfeiture even though disloyalty was substantial.[511] As a result of this equitable discretion, opinions like *Malhotra*, which limited forfeiture to bonuses in addition to actual damages based on embezzlement and fraud,

506. *See* Orkin Exterminating Co. v. Rathje, 72 F.3d 206, 208 (1st Cir. 1995) ("Because of the court's finding that defendant's energies were diverted away from his responsibilities to [the principal], and given the burden on him to prove the value of his services, the court's finding that he was worth everything [the principal] paid him is very hard to credit."); Milwaukee Precision Casting, Inc. v. Hagedorn, 590 N.W.2d 281, No. 96-2294, 1999 WL 8366, at *9 (Wis. Ct. App. Jan. 12, 1999) (per curiam) (unpublished table decision) (affirming the employee should not have to forfeit compensation because the employee's work allowed the employer to enjoy success it would not have otherwise had; consequently, compensation forfeiture would unjustly deprive the employee and unjustly enrich the employer).

507. *See* Tomsic v. Lautieri (*In re* Tri–Star Techs. Co.), 257 B.R. 629, 637–38 (Bankr. D. Mass. 2001) (finding no forfeiture was required since no evidence was presented that "would denigrate the value of the services" provided).

508. *See* Vendo Co. v. Stoner, 321 N.E.2d 1, 14 (Ill. 1974) ("It borders upon the frivolous for defendants to claim a right to retain the compensation which the judgment restored to plaintiff."); *see also* Dowd & Dowd, Ltd. v. Gleason, 816 N.E.2d 754, 771 (Ill. App. Ct. 2004) (holding agents "cannot claim a right to retain the compensation earned while breaching their fiduciary duty" even if there is no "indication that [they] did not work at the efficiency level or with the diligence that they had prior to" their breach).

509. *In re* Marriage of Pagano, 607 N.E.2d 1242 (Ill. 1992).

510. *See id.* at 1249–50 (acknowledging, when an agent breaches a fiduciary duty, the remedy awarded is within the court's equitable discretion; punitive damages can be awarded for such breach, but it is not automatic).

511. *See* Gaffney v. Harmon, 90 N.E.2d 785, 790 (Ill. 1950) (finding the lower court's decision "does not foreclose [the attorney] from being reimbursed for his expenditures and a reasonable compensation for his services . . . but the [lower court's] holding that [the attorney] held the title to the land in question in trust for [the client] was just and proper"); Oil, Inc. v. Martin, 44 N.E.2d 596, 600–01 (Ill. 1942) (reversing the circuit court's decision and ordering all the mineral interests involved be conveyed to the appellant, minus whatever, if anything, was agreed to be given to the appellee for services rendered); *see also* Clinton Imperial China, Inc. v. Lippert Mktg., Ltd., 878 N.E.2d 730, 737–38 (Ill. App. Ct. 2007) (concluding the trial court did not abuse its discretion when it held there was insufficient grounds for forfeiture since the agent "had already performed the most essential part of its duties").

are possible.[512] In *Malhotra*, the federal district judge implied disdain for compensation forfeiture in general, or at least as claimed in that case, which sought nine years of forfeiture.[513]

In *Cameco, Inc. v. Gedicke*,[514] the New Jersey Supreme Court stated the egregiousness of the fiduciary's disloyalty can have an impact on the trial judge's opinion on apportionment.[515] This observation applies widely in the courts of most states. An example of this phenomenon can be seen in the New York case, *William Floyd Union Free School District v. Wright*.[516] In *Wright*, the court determined the former treasurer of the school had rigged the payment system to report him as retired for the purposes of receiving retirement benefits between April 4, 2000, and January 24, 2003, despite the fact that he was still actively working for the system and receiving a salary.[517] The trial court relieved the plaintiff–school district of its obligation to pay the defendant's insurance benefits for a period of ten years.[518] On appeal, the trial court was instructed to modify the order such that the school district was permanently relieved to pay any insurance benefits.[519]

Note that it is not unusual for courts to misunderstand the standard for forfeiture in Section 469 of the Restatement (Second) of Agency, which refers to "wil[l]ful and deliberate breach of his contract of service"[520] and is further defined in Comment b of that section merely as a "serious

512. *See* Bank of Tokyo–Mitsubishi, Ltd. v. Malhotra, 131 F. Supp. 2d 959, 962 (N.D. Ill. 2000) ("[W]hat is *not* called for is the extraordinarily punitive required repayment of [the employee's] total compensation and related fringe benefits.").

513. *Id.* at 961 (stating, in cases of breach of fiduciary duty, compensation forfeiture is not mandated but is left to the discretion of the court; as such, an award of complete disgorgement of compensation and fringe benefits received over nine years of employment is wholly punitive and overstated).

514. Cameco, Inc. v. Gedicke, 724 A.2d 783 (N.J. 1999).

515. *Id.* at 791. Describing what may be considered an egregious affront to one's fiduciary duty, the court explains, "If the employee directly competes with the employer, aids the employer's direct competitors or those with interests adverse to the employer's interests, participates in a plan to destroy the employer's business, or secretly deprives the employer of an economic opportunity, the employee may forfeit the right to compensation." *Id.*

516. William Floyd Union Free Sch. Dist. v. Wright, 877 N.Y.S.2d 395 (App. Div. 2009).

517. *Id.* at 396–97.

518. *Id.* at 396.

519. *Id.*

520. RESTATEMENT (SECOND) OF AGENCY § 469 (AM. LAW INST. 1958) ("An agent is entitled to no compensation for conduct which is disobedient or which is a breach of his duty of loyalty; if such conduct constitutes a wil[l]ful and deliberate breach of his contract of service, he is not entitled to compensation even for properly performed services for which no compensation is apportioned.").

violation of a duty of loyalty."[521]

G. *Non-forfeiture Clauses*

Finally, the issue of non-forfeiture provisions in employment contracts or retainer agreements may grow in prominence as professionals may try to use such provisions to shield their regular compensation as well as their retirement benefits. ERISA issues require specialized expertise beyond that of the author, but non-forfeitability extends beyond ERISA regulations. Basic retirement plans are required to vest and, therefore, are required to be non-forfeitable.[522] However, top hat plans are not required by ERISA to be non-forfeitable, and the dicta of at least two opinions indicates a non-forfeiture clause would have saved those plans as well.[523]

V. OTHER CLAIMS AND REMEDIES

A. *Richard Scrushy: "The CEO of the Fraud"*[524]

Richard Scrushy was the founder of HealthSouth Corp. (HealthSouth), a publicly held company that provided outpatient surgery and rehabilitative healthcare services.[525] To enhance the corporation's executive bonus pool, fifteen or more HealthSouth executives conspired to defraud the public by fabricating accounting statements between 1996 and 2002.[526] As originally reported, each year was profitable in a cumulative amount of $1.26 billion over the seven years.[527] As eventually corrected and restated,

521. *Id.* § 469 cmt. b ("A serious violation of a duty of loyalty or seriously disobedient conduct is a wil[l]ful and deliberate breach of the contract of service by the agent, and . . . the agent thereby loses his right to obtain compensation for prior services, compensation for which has not been apportioned.").

522. *See* Foley v. Am. Elec. Power, 425 F. Supp. 2d 863, 868–71 (S.D. Ohio 2006) (suggesting that vesting ERISA provisions preclude forfeiture).

523. *See Kozlowski I*, 756 F. Supp. 2d 553, 565 (S.D.N.Y. 2010) ("Under federal common law, benefits accrued in top hat plans are assumed to be forfeitable unless otherwise agreed to by the parties to the contract." (quoting Bigda v. Fischbach Corp., 898 F. Supp. 1004, 1016 (S.D.N.Y. 1995), *aff'd*, 101 F.3d 108 (2d Cir. 1996))); *Foley*, 425 F. Supp. 2d at 871 (recognizing, if a top hat plan does not have a non-forfeiture agreement, employers may withhold payments that accrued during the disloyalty).

524. Laurence Viele Davidson & David Beasley, *HealthSouth's Scrushy Liable in $2.88 Billion Fraud*, BLOOMBERG (June 18, 2009, 13:51 EDT), http://www.bloomberg.com/apps/news?pid=newsarchive&sid=a89tFKR4OevM.

525. *Id.*

526. *In re* HealthSouth Corp. S'holders Litig., 845 A.2d 1096, 1102 (Del. Ch. 2003), *aff'd sub nom.* Scrushy v. Biondi *ex rel.* HealthSouth Corp. (*In re* Healthsouth Corp. S'holders Litig.), No. 22, 2004, 2004 WL 835879 (Del. Apr. 14, 2004).

527. *Scrushy I*, 955 So. 2d 988, 1005 (Ala. 2006).

the company's net income was negative in each of those years (except 1996) with cumulative losses of $1.87 billion due to fraudulent entries, accounting changes, and necessary write-downs in asset values.[528]

In 1999, before it was a prohibited practice, Scrushy borrowed $25,218,114 from HealthSouth to buy 4,367,397 shares of HealthSouth common stock at $5.78 per share.[529] In 2002, he proposed to repay the loan ahead of time by tendering 2,506,770 shares of his stock which he represented was worth $10.06, the market price of the stock on July 31, 2002. His buyback transaction was executed on August 1, 2002.[530] Thereafter, the following facts came to light:

- In August 2002 HealthSouth issued a press release announcing that Scrushy had resigned as CEO (but would remain as chairman of the board) and that the company needed to reduce its projections for the year's pre-tax earnings by $175 million.[531]
- On March 3, 2003, HealthSouth announced it needed to make a "write-down" of asset values of $445 million for the fourth quarter of 2002 and "other unusual charges" of $194.8 million. By this time, the stock had fallen to $0.11 from $10.08 on July 31, 2002.[532]
- On March 19, 2003, the Securities and Exchange Commission filed a complaint against HealthSouth, alleging violations of the securities laws.[533]
- At about the same time, the U.S. Attorney for the Northern District of Alabama separately announced Weston Smith, the HealthSouth chief financial officer, had pled guilty to conspiring to falsify the financial statements from 1997 through 2003.[534]
- On March 24, 2003, HealthSouth announced it retained an outside accounting firm to conduct a forensic audit of the company's financial statements.[535]
- On March 25, 2003, the New York Stock Exchange announced the delisting of HealthSouth.[536]

528. *Id.*
529. *In re HealthSouth*, 845 A.2d at 1100.
530. *Id.*
531. *Id.*
532. *Id.* at 1101.
533. *Id.* at 1102.
534. *Id.* at 1101.
535. *Id.*
536. *Id.*

- On March 31, 2003, Scrushy was formally fired.[537]
- On July 7, 2003, the outside auditor provided the company with the preliminary estimate that prior earnings had been overstated by at least $2.5 billion.[538]

This accounting scandal generated two separate series of lawsuits. Criminal charges were filed in April 2003 against Scrushy and a group of HealthSouth executives.[539] In that case, fifteen HealthSouth executives eventually pled guilty to a scheme to generate misleading financial statements for the purpose of enhancing profit sharing compensation.[540] On June 28, 2005, Scrushy was found not guilty.[541] However, he was subsequently indicted on charges of bribery, extortion, and money laundering and convicted in June 2006.[542] He was sentenced to eighty-two months of prison[543] from which he was released on July 25, 2012, after serving seventy-four months.[544]

In 2003, several civil lawsuits were filed as derivative actions.[545] The main action related to the allegation that Scrushy had participated in the accounting fraud and caused huge damages to the operations of HealthSouth and the investing public.[546] Separate claims related indirectly to the main action were allowed to proceed on their own.[547] The first such independent claim related to the buyback transaction, which was

537. *Id.*

538. *Id.*

539. *In re* HealthSouth Corp. S'holders Litig., 845 A.2d 1096, 1102 (Del. Ch. 2003), *aff'd sub nom.* Scrushy v. Biondi *ex rel.* HealthSouth Corp. (*In re* Healthsouth Corp. S'holders Litig.), No. 22, 2004, 2004 WL 835879 (Del. Apr. 14, 2004).

540. *Id.* at 1101.

541. Greg Farrell, *Scrushy Acquitted of All 36 Charges*, USA TODAY (June 28, 2005, 11:20 AM), http://usatoday30.usatoday.com/money/industries/health/2005-06-28-scrushy_x.htm.

542. *See* Davidson & Beasley, *supra* note 524 (acknowledging, in 2006, Scrushy was convicted of bribery for "giving Alabama Governor Don Siegelman a $500,000 campaign contribution in return for a seat on a state hospital regulatory board").

543. Bob Sims, *Siegelman, Scrushy Taken into Custody*, AL.COM (June 28, 2007, 7:20 PM), http://blog.al.com/spotnews/2007/06/siegelman_gets_sevenplus_years.html.

544. Associated Press, *Richard Scrushy Released from Federal Custody*, WTVY (July 26, 2012, 10:28 AM), http://www.wtvy.com/home/headlines/Richard-Scrushy-Released-from-Federal-Custody-163863696.html.

545. Scrushy v. Tucker (*Scrushy II*), 70 So. 3d 289, 294 (Ala. 2011).

546. Claims against Scrushy included: "(1) improper 'interested transactions,' waste and 'misappropriation of corporate assets'; (2) unjust enrichment; (3) breach of contract; (4) conspiracy; (5) 'intentional, reckless, and innocent misrepresentation and suppression'; (6) breach of fiduciary duty of loyalty, related to fraud, false accounting, and 'insider trading'; and (7) seeking to impose a constructive trust." *Id.*

547. *See id.* (suggesting the pending derivative actions proceeded on their own).

heard in the Delaware Chancery Court.[548] The court granted a partial summary judgment motion against Scrushy—which was later affirmed by the Delaware Supreme Court[549]—that rescinded the buyback transaction.[550] The key point in that suit was that Scrushy was found liable on the claim of innocent misrepresentation, which stemmed from Scrushy's statement that the market value on the date of the buyback was a fair representation of its value.[551] Claims of fraud were not alleged, but as CEO, he was held responsible for the filing of grossly misrepresentative accounting statements between 1996 and 2002 and for benefitting from those false accounting statements in the buyback transaction.[552]

In 2006, after Scrushy was acquitted in the first criminal proceedings but also after the HealthSouth executives pled guilty to filing grossly misstated accounting statements, a second motion for partial summary judgment was heard in an Alabama court against Scrushy in which HealthSouth claimed he had been unjustly enriched by being paid $46.7 million of bonus payments between 1996 and 2002 for profits that did not in fact exist.[553] The trial court granted the partial summary judgment motion for the years 1997 through 2002 and ordered disgorgement in the amount of $47.8 million (including prejudgment interest).[554] The Alabama Supreme Court affirmed the order, emphasizing the cause of action for unjust

548. *In re* HealthSouth Corp. S'holders Litig., 845 A.2d 1096, 1102 (Del. Ch. 2003), *aff'd sub nom.* Scrushy v. Biondi *ex rel.* HealthSouth Corp. (*In re* Healthsouth Corp. S'holders Litig.), No. 22, 2004, 2004 WL 835879 (Del. Apr. 14, 2004).

549. Scrushy v. Biondi *ex rel.* HealthSouth Corp. (*In re* Healthsouth Corp. S'holders Litig.), No. 22, 2004, 2004 WL 835879 (Del. Apr. 14, 2004).

550. *In re HealthSouth Corp.*, 845 A.2d at 1101.

551. *Id.* at 1106 ("First, Scrushy represented to HealthSouth that the market price was a reliable way to value his shares, thereby vouching again for the integrity of the financial statements he had signed (and earnings projections he had caused the company to make).").

552. The court expounds on the particular nature of Scrushy's fiduciary relationship with HealthSouth, noting

> the CEO of a major corporation like HealthSouth possesses an enormous amount of authority and therefore owes the corporation a corresponding degree of responsibility. HealthSouth's board of directors was entitled to rely upon Scrushy and his management team, particularly in the preparation of the company's financial statements, an area in which management has traditionally been preeminent. In the process of preparing and signing financial statements, Scrushy necessarily represented to the company's board, audit committee, outside auditors, and its public stockholders that the financial statements his management team had prepared were materially accurate in all respects. As the auditor's report for HealthSouth's FY 2001 10-K stated: "These financial statements and schedule are the responsibility of the Company's management."

Id. at 1107 (citation omitted).

553. *Scrushy I*, 955 So. 2d 988, 1002–03 (Ala. 2006).

554. *Id.* at 1005.

enrichment in Alabama and Delaware does not require or presuppose the defendant did anything wrong or dishonest.[555]

After the two partial summary judgments were granted and affirmed by their respective state supreme courts, and after Scrushy was first acquitted and then convicted of various felonies, the main civil case—in which Scrushy was alleged to have been involved in the accounting fraud—proceeded, which eventually led to the trial judge calling Scrushy "the CEO of the fraud."[556]

It is ironic that the largest judgment for compensation forfeiture ($27 million) was also the least significant (less than 1%) to the overall judgment. While Scrushy did appeal the judgment for compensation forfeiture, his assertions were, strangely, based on his claim that compensation forfeiture would only be warranted upon an order to rescind his employment agreements.[557] The Alabama Supreme Court pointed out the plaintiffs had pled a claim for breach of fiduciary duty for which they sought the remedy of compensation forfeiture.[558]

As a case relating to compensation forfeiture, the Scrushy opinion seems weak due to the unusually weak defense.[559] The claims for innocent misrepresentation and unjust enrichment seem much more interesting and applicable in the future against other examples of innocent misrepresentation by senior executives, or in cases in which one cannot prove the defendant caused an obvious benefit.

B. *Asset Forfeiture*

In 2010, the Texas Supreme Court affirmed a new variation of compensation forfeiture that is intended to be used when a fiduciary breaches her fiduciary duty to the principal in the course of an asset transaction.[560] It held, "[W]here willful actions constituting breach of fiduciary duty also amount to fraudulent inducement, the contractual

555. *See id.* at 1012 (concluding, under Alabama and Delaware law, "Scrushy was unjustly enriched by the payment of the bonuses, which were the result of the vast accounting fraud perpetrated upon HealthSouth and its shareholders, and . . . . [i]t would be unconscionable to allow [him] to retain . . . [the bonuses] at the expense of the corporation").

556. Davidson & Beasley, *supra* note 524.

557. *Scrushy II*, 70 So. 3d 289, 305 (Ala. 2011) ("The gravamen of Scrushy's argument is that the remedy of disgorgement derives solely from equitable rescission. However, it is evident that the trial court 'also' ordered the repayment as 'damages for [Scrushy's] breach of the duty of loyalty.'").

558. *Id.* at 305–06.

559. *Id.* at 306 (holding Scrushy "waived a challenge to this aspect of the judgment" because he "relie[d] exclusively on his equitable-rescission argument").

560. *See Swinnea II*, 318 S.W.3d 867, 873 (Tex. 2010) (affirming equitable forfeiture for a breach of fiduciary duty).

consideration received by the fiduciary is recoverable in equity regardless of whether actual damages are proven, subject to certain limiting principles set out below."[561] So if one partner proposes a transaction based in fraud and a willful breach of fiduciary duty, the remedy would be to reverse the transaction, except the partner in breach loses the consideration that he conveyed in the exchange (in addition to possible compensatory damages, lost profits, and punitive damages).[562]

In *ERI Consulting Engineers, Inc. v. Swinnea*,[563] the two parties, Snodgrass and Swinnea, were equal shareholders in an environmental consulting business, ERI Consulting Engineers, Inc. (ERI), and in a holding company that owned the headquarters property, Malmeba Co., (Malmeba).[564] In 2001, Swinnea sold his interest in ERI to Snodgrass and agreed not to compete with ERI for six years in exchange for $497,500 and Snodgrass's interest in Malmeba.[565] Evidence was presented at the bench trial that showed Swinnea prepared to compete with ERI even before the transaction agreement was executed and even though Swinnea continued to work full time for ERI. It was shown that Swinnea expected to be able to buy ERI later for a depressed price after competition from his new company had "run [ERI] into the ground."[566]

The trial court awarded ERI and Snodgrass lost profits of $300,000, asset forfeitures of $437,500 (part of the $497,500 paid to acquire Swinnea's interest in ERI), $150,000 ("the value of Snodgrass's one-half interest in Malmeba transferred to Swinnea"), $133,200 ("the sum of the lease payments from ERI to Malmeba after the buyout"), and $1 million in exemplary damages.[567] The twelfth district reversed the trial court, holding Snodgrass take nothing as the lost profits were not sufficiently proven and the precedents for fee forfeiture did not justify the authority to forfeit assets.[568] The supreme court reversed the court of appeals and affirmed the trial court's award (except for an adjustment to the amount of

561. *Id.*

562. *See id.* at 874 ("Although forfeiture of contractual consideration may 'have a punitive effect' like forfeiture of compensation . . . it may nevertheless be necessary to protect fiduciary relationships.").

563. ERI Consulting Eng'rs, Inc. v. Swinnea (*Swinnea II*), 318 S.W.3d 867 (Tex. 2010).

564. *Id.* at 870–71.

565. *Id.*

566. *Id.* at 871.

567. *Id.* at 871–72.

568. *See* Swinnea v. ERI Consulting Eng'rs, Inc. (*Swinnea I*), 236 S.W.3d 825, 841 (Tex. App.—Tyler 2007), *pet. granted, aff'd in part*, *rev'd in part*, 318 S.W.3d 867 (Tex. 2010) (finding the line of cases justifying fee forfeiture did not apply because there was no fiduciary fee and the appellees did not prove any reasonably certain lost profits).

lost profits): "The main purpose of forfeiture is not to compensate an injured principal . . . . Rather, the central purpose . . . is to protect relationships of trust by discouraging agents' disloyalty."[569]

Asset forfeiture, however, flouts most of the safeguards that prevent remedies in equity from exacting punitive measures. For example, asset forfeiture rejects counter-restitution; and therefore, the remedy can easily exceed the defendant's gain, thereby breaching the protection implied in *Snepp*.[570] The fiduciary that makes a substantial cash outlay to purchase or improve an asset that is subsequently forfeited is penalized in an amount that can be greater than any profit or benefit.[571]

Just as the state supreme court's opinion in *Burrow v. Arce*[572] spurred more claims for fee forfeiture against lawyers, its subsequent opinion in *Swinnea*[573] increased the number of claims for compensation forfeiture in the Texas courts. However, given the shaky foundation for *Swinnea*'s extension of fee or compensation forfeiture to asset forfeiture, some of the new Texas appellate opinions appear to be outliers compared to the overall application of compensation forfeiture. One such outlying opinion was handed down in *Saden v. Smith*,[574] which correctly held the trial court could not award actual damages for both breach of contract and breach of fiduciary duty against an equal shareholder for disloyal competition because only one cause of action applied.[575] In addition to awarding lost profits for breach of contract, the court also awarded disgorgement of the errant fiduciary's profits to deter breaches of fiduciary duty.[576] The result

569. *Swinnea II*, 318 S.W.3d at 873 (quoting Burrow v. Arce, 997 S.W.2d 229, 238 (Tex. 1999)).

570. *Snepp* forwards "the remedy reaches only funds attributable to the breach[;] it cannot saddle the [fiduciary] with exemplary damages out of all proportion to [the] gain." Snepp v. United States, 444 U.S. 507, 515–16 (1980) (per curiam).

571. *See* ANDREW BURROWS, THE LAW OF RESTITUTION 250 (3d ed. 2011) (1992) ("Though the defendant has been fraudulent, he must not be robbed, nor must the plaintiff be unjustly enriched, as he would be if he both got back what he had parted with and kept what he had received in return." (citation omitted)); *see also* Clarke v. Dickson (1858) 120 Eng. Rep. 463, 465 ("If you are fraudulently induced to buy a cake you may return it and get back the price; but you cannot both eat your cake and return your cake.").

572. Burrow v. Arce, 997 S.W.2d 229, 244 (Tex. 1999) (allowing forfeiture where other remedies do not fully compensate the client).

573. *See Swinnea II*, 318 S.W.3d at 873 (holding breach of duty of loyalty means a lawyer is not entitled even to compensation for that which he properly performed).

574. Saden v. Smith, 415 S.W.3d 450, 470 (Tex. App.—Houston [1st Dist.] 2013, pet. denied).

575. *See id.* at 469 ("[A]llowing the recovery of actual damages for both breach of contract and breach of fiduciary duty violates the one-satisfaction rule, and is therefore error.").

576. *Id.* The compensation and personal expenses of the fiduciary and equal shareholder were not eligible for forfeiture because they had not been expensed by the plaintiff's expert in determining the plaintiff's lost profits. *Id.* at 466–67.

was that the court of appeals held the fiduciary was liable for $941,907 in lost profits for breach of contract and an additional $941,907 in disgorgement of the defendant's profits, rejecting the defendant's objections that the award was duplicative.[577] The court clearly mistook profit disgorgement for compensation forfeiture, but the potential expansiveness of *Swinnea* surely encourages this mistake.

Other Texas cases apply compensation forfeiture in their own "different way." In a case against the former president of a company for disloyal compensation, the Fifth Circuit affirmed an award of $342,117 for breach of contract, which amounted to 100% of the fiduciary's compensation during the period of disloyalty and the plaintiff's lost profits for breach of fiduciary duty.[578] In *Dernick Resources, Inc. v. Wilstein*,[579] the judge correctly added compensation forfeiture to lost profits.[580] The interesting aspect in *Dernick* is that the trial judge awarded actual damages of only $162,000 compared to forfeiture of $1.7 million (until the appeals court added another $750,000 of actual damages).[581] The court in *McCullough v. Scarbrough, Medlin & Associates., Inc.*,[582] held the plaintiff was entitled to choose between treatment as breach of contract or breach of fiduciary duty and specifically did not allow the breach of contract claim to add on forfeiture.[583] Note however, the breach of fiduciary duty approach allowed a claim for actual damages, disgorgement, and forfeiture.[584]

C. *Fiduciary Claims Against Lawyers*

Claims for breach of fiduciary duty against lawyers, one of the oldest applications of the claim,[585] will not be separately addressed in this Article. There appears, however, to be a related issue that should be acknowledged. When former clients sue their lawyers for breach of

577. *Id.* at 468–69.

578. Advanced Nano Coatings, Inc. v. Hanafin, 556 F. App'x. 316, 318 (5th Cir. 2014).

579. Dernick Res., Inc. v. Wilstein, No. 01-13-00853-CV, 2015 WL 3981772 (Tex. App.—Houston [1st Dist.] June 30, 2015, no pet.).

580. *Id.* at *13 (affirming trial court's award of both actual damages from lost profits and fee forfeiture); *see also* White v. Pottorff, No. 05-14-00675-CV, 2015 WL 4914726, at *7 (Tex. App.—Dallas Aug. 18, 2015, no pet.) (affirming the award of $375,000 for compensation forfeiture).

581. *Denrick*, 2015 WL 3981772, at *4, *24.

582. McCullough v. Scarbrough, Medlin & Assocs., Inc. 435 S.W.3d 871 (Tex. App.—Dallas 2014, pet. denied).

583. *Id.* at 917.

584. *Id.*

585. *See* Silbiger v. Prudence Bonds Corp., 180 F.2d 917, 920–21 (2d Cir. 1950) (showing historically, "the usual consequence" for disloyal attorneys was "a forfeiture of all pay" (citing Shire v. King (1603) 80 Eng. Rep. 24)).

fiduciary duty and legal malpractice, many states effectively recognize a form of pre-emption that acts to dismiss the fiduciary claim on summary judgment. In Texas, between 1988 and 2012, defendant–attorneys in 60% of cases with both claims were granted summary judgment for breach of fiduciary duty (77% of those dismissals were upheld on appeal).[586] By comparison, in Texas, between 1988 and 2012, defendant–non-attorneys in only 36% in cases with both claims were granted summary judgment for breach of fiduciary duty, and 66% of those dismissals were affirmed.[587] The specific rationale in Texas is called "fracturing."[588] There has been a surge in Texas, and the rest of the country, in claims against lawyers for legal malpractice and breach of fiduciary duty. The surge for legal malpractice has subsided, but the surge in claims for breach of fiduciary duty continues. Courts in Texas perceived many of the claims for breach of fiduciary duty were nothing more than the same claim for legal malpractice repeated as claims for breach of fiduciary duty or sometimes fraud. The fracturing defense has had such a marked impact on litigation against lawyers that the liability rate for lawyers is markedly lower than for non-lawyer–defendants.[589] Other states readily dismiss claims for breach of fiduciary duty against lawyers under the similar defense of duplicativeness.[590]

Case opinions that affirm summary judgment dismissals under fracturing or duplicativeness fail to explain how the defense complies with the notion of pleading in the alternative or why such defenses should not follow the standard in federal procedure for the defense of redundancy.[591] More importantly, even if the doctrine of duplicativeness or fracturing were fully supported in legal doctrine, no court opinions have explained why the plaintiff should not be allowed to choose whether to have the malpractice or fiduciary duty claim dismissed nor how a claim for fiduciary

586. Roach, *supra* note 6, at 387.

587. *Id.*

588. *Id.* at 435–46.

589. *See id.* at 449 (concluding, out of fifty-two cases with claims for breach of fiduciary duty against a lawyer in which the fracturing defense was used, no defendants were found liable; five cases were remanded, forty-five were affirmed for dismissing the claim, and two were reversed on appeal).

590. *E.g.*, Weil, Gotshal & Manges, LLP v. Fashion Boutique of Short Hills, Inc., 780 N.Y.S.2d 593, 596 (App. Div. 2004) ("As to the claim for breach of fiduciary duty, we have consistently held that such a claim, premised on the same facts and seeking the identical relief sought in the legal malpractice cause of action, is redundant and should be dismissed.").

591. *See* Hardin v. Am. Elec. Power, 188 F.R.D. 509, 511 (S.D. Ind. 1999) ("[M]ere redundancy or immateriality is not enough to trigger the drastic measure of striking pleading or parts thereof; in addition, pleading must be prejudicial to the defendant." (citing Talbot v. Robert Matthews Distrib. Co., 961 F.2d 654, 664 (7th Cir. 1992))).

duty can be duplicative of a claim for legal malpractice that is otherwise being simultaneously dismissed on other grounds.

However, the important point is that a cause of action for breach of fiduciary that seeks the remedy of compensation forfeiture or fee forfeiture is treated differently and not as readily dismissed as fiduciary claims that seek damages. Cases for breach of fiduciary duty have survived the defense of duplicativeness because the claimant is seeking a different remedy than the damages claim for legal malpractice.[592] In Texas, despite the supreme court precedent that specifically reversed the dismissal of the plaintiff's causes of action for legal malpractice and breach of fiduciary duty for fee forfeiture, the trial courts and courts of appeals have found new grounds for dismissing such claims,[593] but some claims have survived.[594]

Claims for fee forfeiture in Texas have been most successful in two class action cases. In *Burrow v. Arce*,[595] the state supreme court reversed the appeals court and denied the lawyer–defendant's motion for summary judgment on the claims for malpractice and breach of fiduciary duty regarding a class action in which the lawyer gained contingency fees of $60 million.[596] The case against the law firm of John O'Quinn P.C. went to arbitration, and the panel in that case awarded forfeiture of $25 million out of total fees of $253.4 million.[597]

592. *See* Ulico Cas. Co. v. Wilson, 843 N.Y.S.2d 749, 762 (Sup. Ct. 2007) ("It is well settled that '[o]ne who owes a duty of fidelity to a principal and who is faithless in the performance of his services is generally disentitled to recover his compensation, whether commissions or salary.'" (alteration in original) (quoting Feiger v. Iral Jewelry, Ltd., 363 N.E.2d 350, 351 (N.Y. 1977))), *aff'd as modified*, 865 N.Y.S.2d 14 (App. Div. 2008).

593. *See* Roach, *supra* note 6, at 447–48 (describing appellate courts' marginalization of the fee forfeiture remedy as used against lawyer–fiduciaries).

594. *See* Yaquinto v. Segerstrom (*In re* Segerstrom), 247 F.3d 218, 225 n.5 (5th Cir. 2001) ("[W]hile the Texas Supreme Court has dispensed with the need to prove an actual injury and causation, . . . injury and causation are still required when a plaintiff seeks to recover damages for a breach of fiduciary duty." (citing Burrow v. Arce, 997 S.W.2d 229, 240 (Tex. 1999))); *see also* Balestri v. Hunton & Williams, LLP (*In re* Hallwood Energy, LP), No. 3:11-CV-3359-G, 2014 U.S. Dist. LEXIS 130481, at *2–3 (N.D. Tex. Sept. 17, 2014) ("Summary judgment/judgment on the pleadings is denied on count two (breach of fiduciary duty), but the plaintiff's remedy, in the event that liability is found, is limited to possible fee forfeiture."); Gammon v. Hodes, No. 03-13-00124-CV, 2015 WL 1882274 at *1, *9 (Tex. App.—Austin Apr. 24, 2015, pet. denied) (affirming the take nothing judgment for the lawyer's collection action, forfeiture of additional $23,379 of paid lawyer's fees, and the denial of the lawyer's claim for quantum meruit due to the breach of fiduciary duty owing to an unreasonable retainer agreement executed after representation had been initiated).

595. Burrow v. Arce 997 S.W.2d 229 (Tex. 1999).

596. *Id.* at 232.

597. John M. O'Quinn PC v. Nat'l Union Fire Ins., 33 F. Supp. 3d 756, 774 (S.D. Tex. 2014). In the appellate opinion that affirmed the denial of malpractice coverage for the damages and

VI. CONCLUSION

Compensation forfeiture does not require testimony from an expert nor extensive motion practice on causation.[598] If the former employee has been convicted of a related crime, liability for breach of fiduciary duty seems likely on a summary judgment basis. For the employer, pleading for compensation forfeiture is a low-risk, low-cost litigation tactic to increase the size of the remedy for a given set of claims and facts about the defendant's actions.

The dual goals for breach of fiduciary duty lead to multiple remedies for a single cause of action, including a remedy at law and a remedy in equity. When applicable, compensation forfeiture is stacked on top of the first two remedies without any offsets or adjustments, or it can be implied in the measure of disgorgement. The result of a plea for compensation forfeiture is subject to the discretion of the trial judge who may or may not resist the remedy as excessive despite the evidence of serious disloyalty and egregiousness.

The underlying legal theory for compensation forfeiture as a deterrent to disloyalty suffers from two unproven assumptions. First, it seems unlikely that many employees are aware of their potential liability for disloyalty. Second, from a very limited sample of executives that got caught, it appears that executives that are substantial violators of the duty of loyalty are also substantially irrational and not likely to be influenced by rational deterrence.[599]

This Article does not conclude or imply that compensation forfeiture is necessarily punitive as it is the simplest form of disgorgement or measure

forfeiture awarded against the law firm, the underlying claim for breach of fiduciary duty, styled *Wood v. John M. O'Quinn, PC*, "was filed in . . . 1999 and ordered to arbitration in 2004." *Id.* at 758 n.1. The arbitration panel's award was described as follows:

> On September 26, 2007, the Panel issued a final arbitration award . . . . [which] held the O'Quinn Firm liable for damages totaling . . . [$41,465,950], in the following specific amounts: (1) . . . [$9,979,364], for breach of contract; (2) . . . [$2,494,841], for attorneys' fees on the breach of contract claim; (3) . . . [$3,991,745], in interest on the breach of contract damages; and (4) . . . [$25 million], and other related relief. On October 12, 2007, the Rusk County court entered a final judgment confirming the Final Award in all respects. On December 4, 2009, the O'Quinn Firm, on its own, settled the Final Award for $46.5 million.

Id. at 762 (citations omitted).

598. *See* Floyd v. Hefner, 556 F. Supp. 2d 617, 661 (S.D. Tex. 2008) ("Where a plaintiff seeks the remedy of fee forfeiture and proves his claim of breach of fiduciary duty, there is no requirement that he must prove causation . . . ." (citing Arce v. Burrow, 958 S.W.2d 239, 248–49 (Tex. App.—Houston [1st. Dist.] 1997, pet. granted))).

599. However, to be fair, deterrence itself would be very difficult to prove in either a positive or negative sense.

of unjust enrichment. Furthermore, remedy packages for breach of fiduciary duty that stack punitive damages on top of compensatory damages and disgorgement are not necessarily disproportionately punitive, but the reasonable limits or safeguards on punitive damages for such packages have not been established for our merged court systems.

At present, the traditional constraints on remedies in courts at law or courts in equity do not operate effectively in our merged courts. Whether or not a remedy package would be disproportionately punitive is, therefore, increasingly dependent on the discretion of the trial judge. Given the prominence of egregious case facts and the likelihood that some of these stacked awards will financially ruin the defendant, these combined remedies seem destined to yield outcomes that are contrary to the traditional sensitivities of either courts at law or courts in equity.

Appendix 1

Stacking Remedies For Breach of Fiduciary Duty

		Total Damages B	Compensating Damages C	Consequential Damages D	Lost Value E	Lost Profits F	Disgorgement G	Compensation Forfeiture H	Punitive Damages I	(H + I)/B	(H+I)/(C+D+E+F+G)
Dowd & Dowd, Ltd. v. Gleason, 816 N.E.2d 754 (Ill. App. Ct. 2004).		2,864,889				1,652,029		812,860	400,000	42%	0.7
HTS, Inc. v. Boley, 954 F. Supp. 2d 927 (D. Ariz. 2013).		179,473	36,991					88,937	53,545	79%	3.9
Levy v. Markal Sales Corp., 643 N.E.2d 1206 (Ill. App Ct. 1994).		5,252,248	553,130					1,699,118	3,000,000	89%	8.5
Purolator Prod., Inc. v. Tonte Indus., Inc., 413 F.2d 989 (9th Cir. 1969).		31,236	12,982					10,754	7,500	58%	1.4
Vendo Co. v. Stoner, 321 N.E.2d 1 (Ill. 1974).		7,345,000			5,039,165	2,135,000		170,835		2%	0.02
Yiba--Tech Eng'rs, Inc. v. Kawalek, 849 F. Supp. 2d 462 (D.N.J. 2012).		3,390,054	16,962				2,045,094	197,980	1,130,018	39%	0.6
Enstar Group Inc. v. Grassgreen, 812 F. Supp. 1562 (M.D. Ala. 1993).	a	17,147,000	1,618,053	328,947				5,200,000	10,000,000	89%	9.4
Aramony v. United Way of Am., 28 F. Supp. 2d 147 (S.D.N.Y. 1998), *aff'd in part, rev'd in part sub nom.* Aramony v. United Way Replacement Benefit Plan, 191 F.3d 140 (2d Cir. 1999).	b	2,321,944	357,889				1,914,055	50,000	85%	5.5
Aetna USA, Inc. v. Eldelman, 914 N.E.2d 36 (Mass. 2009).		7,819,812	1,040,812					6,779,000		87%	6.5
ICD Pub'ns, Inc. v. Gittlitz, 2014 IL App (1st) 133277.		9,242,280	1,220,623					6,021,657	2,000,000	87%	6.6
Average										66%	4.3
Swinnea v. ERI Consulting Eng'rs, Inc., 364 S.W.3d 421, 424–25 (Tex. App.—Tyler 2012, pet. denied).	c	1,899,301	178,601					720,700	1,000,000	91%	9.6

Notes

a Figures shown do not include any credit for constructive trust or specific restitution

b Figure for compensation forfeiture includes $ 300,000 for forfeiture of 'top hat' retirement plan.

c Figure for compensation forfeiture is actually asset forfeiture. See Section V B