SPRING 2021

STETSON LAW REVIEW FORUM

On Measuring Damages Where a Contract Breach Benefits the Promisee: Response to Mark Giancaspro, *Quantifying Damages in Cases of Advantageous Breach: The Curious Case of McDonald's Milkshakes*

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I. INTRODUCTION

As someone who has regularly taught both contracts and remedies for the past decade and a half, I read with great interest Dr. Giancaspro's article, *Quantifying Damages in Cases of Advantageous Breach: The Curious Case of McDonald's Milkshakes*. I would strongly recommend this article to anyone interested in exploring one of the more fascinating issues that arises at the intersection of these two subject areas: that of ascertaining the damages for a party who "suffers" (if one can call it that) an "advantageous breach" of contract. This issue has long held a particular fascination for me because, on the one hand, if one focuses on the contractual duty owed to the promisee, it seems that she has, in fact, clearly suffered a wrong when the promisor breached his promise to her. On the other hand, of course, the promisee turns out to have profited quite nicely from this "wrong," making any "damages" due her problematic under the traditional principles of compensation embraced by American contract law.[1] As both a lecturer (at the Law School at the University of Adelaide) and a practicing attorney, Dr. Giancaspro has written an article that deftly explores this area by way of an entertaining case study involving the McDonald brothers and Ray Kroc. His article should prove valuable to academicians, judges, practitioners, and anyone else seeking "guidance as to the remedial consequences that may flow from advantageous breaches."[2]

II. THE MCDONALD'S CASE STUDY

Dr. Giancaspro begins his article by using a case study from the McDonald's franchise saga, as recently told in the biographical film, *The Founder* (2016).[3] Many

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1 *See infra* pt. III.

2 Mark Giancaspro, *Quantifying Damages in Cases of Advantageous Breach: The Curious Case of McDonald's Milkshakes*, 48 STETSON L. REV. 70, 70 (2018).

3 *Id.* at 70 (citing THE FOUNDER (FilmNation Entm't 2016)).

people know, in rough outline at least, the general story about the rapid rise of this iconic fast-food chain. Its success skyrocketed after Ray Kroc, a traveling salesman, met with the McDonald brothers and convinced them to let him franchise their restaurant, in exchange for a small percentage of the gross sales for the use of the McDonald's name and brand.[4] What many people (like myself) probably did not know, however, unless they watched the film or read about it, was how cutthroat and unsavory an individual Mr. Kroc was in his dealings with the McDonald brothers, and (for those who care) how interesting were the contractual issues created by Mr. Kroc's opportunistic breach of the franchise agreement he had with the brothers.[5]

In his article, Dr. Giancaspro explains how, after opening an incredible two hundred McDonald restaurants in a short span between 1955 and 1960, Ray Kroc and his franchisees became painfully aware of how expensive it was to run the walk-in coolers needed to store the ice cream used to make McDonald's milkshakes pursuant to the master business model agreed to by the parties.[6] Therefore, Mr. Kroc set about finding a solution to this problem, and was soon given one by a husband-wife team who ran one of the franchises. They suggested that the milkshakes could be made using a product called "Inst-A-Mix," which is a powdered milk that, with the use of "[t]hickening agents and emulsifiers," could "simulate the texture of [ice-cream]" with no discernable difference in taste.[7] After trying a vanilla version of this powdered milkshake, Mr. Kroc was impressed, and set about trying to convince the McDonald brothers to substitute these "Inst-A-Mix" shakes for the real thing.[8]

Unfortunately for Mr. Kroc, the McDonald brothers were nowhere near as enthused about his powdered milkshakes as he was.[9] In fact, when he made his pitch to the brothers, emphasizing the fact that that they could save a lot of money in refrigeration costs and boost their profits through this substitution,[10] the brothers were not only uninterested but actually indignant at the suggestion.[11] In fact, one of the brothers, Dick, sarcastically told Mr. Kroc that if McDonald's were to go down the road of making "milk" shakes with no milk, why not "put sawdust in the hamburgers while we're at it?" and perhaps even start using "Frozen French fries!"[12] Unfortunately for the McDonald brothers, and despite both the franchise agreement

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[4] Giancaspro, *supra* note 2, at 70–71 (citing *Macca's Story*, MCDONALDS AUSTL., https://mcdonalds.com.au/about-maccas/maccas-story (last visited Mar. 18, 2021)).
[5] *Id.* at 73–75.
[6] *Id.* at 71.
[7] *Id.* at 71–72.
[8] *Id.* at 72.
[9] *Id.* at 73.
[10] *Id.* at 72–73.
[11] *Id.* at 73.
[12] *Id.* One cannot help but smile at what Dick McDonald supposed was an argumentum ad absurdum about using frozen fries. Poor guy. Alas, at least he had it right (I think) concerning the absurdity of adding sawdust to the hamburger meat.

between the parties and this conversation between them, the financial savings were just too tempting for Mr. Kroc to pass up, and he soon began shipping out the powdered milkshake mix to all of the franchises except for the San Bernardino store owned and operated by the McDonald brothers, and in clear breach of the parties' franchise agreement.[13]

Given the fact that substitution of a powdered mix for real ice cream was specifically proposed (and rejected) by the McDonald brothers, Mr. Kroc's perfidy seems even worse than, if you will excuse the pun, the plain vanilla breach of contract it would have been had this conversation never taken place. In any event, Dick McDonald was livid when he learned about Mr. Kroc's breach, and, in a telephone conversation expressing his displeasure,[14] specifically told Mr. Kroc that he had "no right" to make such a substitution and was to "stop this instant."[15] When Dick asked Mr. Kroc whether he had made himself "clear," Mr. Kroc flippantly responded "Nah."[16] Incredulously, Dick asked him, "What the hell's that mean?" and told him that he "will abide by the terms of your deal[,]"[17] to which Mr. Kroc responded, "I'm through taking marching orders from you," and accused Dick of "cower[ing] in the face of progress."[18] The conversation only deteriorated from here, with Dick making fun of Mr. Kroc for conflating progress with offering powdered milkshakes[19] and Mr. Kroc calling the McDonald brothers "two yokels"[20] before the following even more lovely exchange took place:

> "Dick: [What?] You will do as we say.
> Kroc: Nope.
> Dick: You have a *contract*.
> Kroc: Contracts are like hearts. They're made to be broken."[21]

Despite the McDonald brothers threatening legal action, Mr. Kroc persisted undeterred, and the brothers eventually capitulated and agreed to a buyout.[22]

[13] *Id.*
[14] *Id.* at 73–74.
[15] *Id.* at 74.
[16] *Id.*
[17] *Id.*
[18] *Id.*
[19] *Id.*
[20] *Id.*
[21] *Id.* (citing THE FOUNDER, *supra* note 3).
[22] *Id.* at 75.

III. ASSESSING CONTRACT DAMAGES WHERE A PROMISEE BENEFITS

Dr. Giancaspro uses these facts as a jumping off point to assess how the McDonald brothers' damages *would* have been measured had they sued Mr. Kroc, given the rather unusual fact that Mr. Kroc's breach increased the profitability of the franchises and thereby directly benefited the brothers.[23] He begins by covering common ground, such as the shibboleth memorized by every first-year contracts student that contract damages are designed to put the injured party in the position she would have occupied but for the breach,[24] and that this is typically done by protecting her expectation,[25] reliance,[26] or restitution interests.[27]

In law and economics parlance, the damages awarded should make the promisee indifferent between performance, on the one hand, or breach plus a payment of money damages, on the other; but in no event should the breach cause the promisee to be made worse (or better!) off.[28] Of course, when one thinks about contract

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[23] *Id.*

[24] *Id.* at 76; *see also* E. ALLAN FARNSWORTH, CONTRACTS § 12.1, 730 (4th ed. 2004) (noting that courts use contract remedies to "put [the injured] party in as good a position as it would have been in had the contract been performed[.]"); U.C.C. § 1-305(a) (2001) ("[R]emedies provided" under the Code are designed to ensure that "the aggrieved party may be put in as good a position as if the other party had fully performed . . . .").

[25] Expectation damages are those damages needed to put the promisee in the position she would have occupied had the promisor performed his contract. *See* FARNSWORTH, *supra* note 24, § 12.1, 730 (noting that the "interest" designed to "put [the injured] party in as good a position as it would have been in had the contract been performed . . . . is called the *expectation interest* and is said to give the injured party the 'benefit of the bargain.'"); *see also* Giancaspro, *supra* note 2, at 77.

[26] Reliance damages are those damages needed to put the promisee in the position she occupied before entering into the contract with the promisor. *See* FARNSWORTH, *supra* note 24, § 12.1, 732 (a court invoking the reliance interest would "attempt to put the injured party back in the position in which that party would have been had the contract not been made."); *see also* Giancaspro, *supra* note 2, at 77.

[27] Restitution damages are those damages designed to measure the gain needed to be taken away from one party to prevent unjust enrichment. *See* FARNSWORTH, *supra* note 24, § 12.1, 733 ("[T]he object of restitution is not the enforcement of a promise, but an entirely distinct goal—the prevention of unjust enrichment" wherein "[t]he focus is on the party in breach rather than on the injured party, and the attempt is to put the party in breach back in the position in which that party would have been had the contract not been made."); *see also* Giancaspro, *supra* note 2, at 77.

[28] *See, e.g.*, Richard Craswell, *Contract Remedies, Renegotiation, and the Theory of Efficient Breach*, 61 S. CAL. L. REV. 629, 636 (1988) ("The stated goal of contract damages is . . . 'to put the plaintiff in as good a position as he would have been in had the defendant kept his contract.' In economic analysis, this is usually translated as . . . the amount necessary to

"damages," one hardly has in mind the atypical (and, in practice, rather rare[29]) example of a promisee *benefiting* from the promisor's breach,[30] probably for the simple reason that parties who benefit financially from technically legal "wrongs" rarely sue, being less interested in the principle of the matter than in whether they come out on the red or the black side of the ledger. Of course, this is exactly what happened when Mr. Kroc's breach caused the McDonald brothers' profits to *increase*. The question, of course, is how, if at all, a court should deal with such a problem where it arises?

One approach, discussed by Dr. Giancaspro, is by realizing that although the McDonald brothers ostensibly benefited "by way of reduced costs,"[31] they may, in fact, have suffered at least two types of injuries to their expectation interest. The first type of injury they may have suffered is the lost profits that *could* have resulted once customers became aware of their practice of serving powdered milkshakes in lieu of the real thing.[32] Not only was there no evidence of this in the case study,[33] but even if public opinion did turn against the McDonald's franchise for such a practice, such damages would be extremely difficult to prove, given that damages must generally be proven with "reasonable certainty" to be recoverable.[34] The second type of injury the McDonald brothers might have suffered would be for their "disappointment and distress following a contract breach."[35] However, these damages are even more difficult to prove than the first, and even where provable, are typically only allowed if "the contract or the breach is of such a kind that serious emotional disturbance was a particularly likely result."[36] I am not sure whether this rather high bar could be cleared in the McDonald's case study in most American courts, though perhaps it could be, given the conversation that took place between Mr. Kroc and Dick McDonald prior to Mr. Kroc's breach.[37]

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leave the plaintiff absolutely indifferent, in subjective terms, between having the defendant breach and pay damages or having the defendant perform." (quoting Hawkins v. McGee, 84 N.H. 114, 117 (1929))); *see also* Giancaspro, *supra* note 2, at 83.

[29] Though rare, these cases do come up, and numerous examples of such breaches are discussed by Dr. Giancaspro in his article at pages 79–86, often in cases where the promisee's damages are offset due to some corresponding gain, which must be taken into account by way of the doctrine of mitigation. *See* Giancaspro, *supra* note 2, at 79–86.

[30] *Id.* at 79.

[31] *Id.* at 87.

[32] *Id.*

[33] *Id.*

[34] *See* RESTATEMENT (SECOND) OF CONTRACTS § 352 (AM. LAW INST. 1981).

[35] Giancaspro, *supra* note 2, at 87.

[36] *See* RESTATEMENT (SECOND) OF CONTRACTS § 353.

[37] Dr. Giancaspro has a nice discussion of this point in his article, as when he writes, on the one hand, that although "[i]t is obvious from the conversations that transpired between Dick and Mac following Kroc's breach of the franchise agreement that they were deeply

Dr. Giancaspro also discusses a possible claim one of the brothers may have pursued against Mr. Kroc for physical damages when he "collapsed to the floor and was rushed to the hospital" from a diabetic attack upon learning that Mr. Kroc had used their family name "without their permission to head Kroc's franchising business."[38] I have to admit that such a damages claim for *breach of contract* would not readily have occurred to me because (with a few rare exceptions, such as breaches of contract that are committed alongside an independent tort)[39] these damages are not routinely awarded by courts in U.S. contract law outside of a few well-recognized exceptions.[40] In any event, Dr. Giancaspro suggests that such a claim would be unlikely to overcome[41] two arguments that would almost certainly be brought up by Mr. Kroc's lawyers: that such damages, to be recoverable, must be *caused* by the breach and cannot be sufficiently *remote*,[42] i.e., that such damages must be foreseeable as a probable consequence of the breach.[43]

Dr. Giancaspro then briefly considers (1) a damages claim for loss of reputation, which would have to overcome the issues of causation and remoteness discussed above; and (2) a claim for exemplary or punitive damages to punish Mr. Kroc for his unsavory behavior, which, as he rightly points out, would almost

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distressed and disappointed by this behavior given that it resulted in changes to their traditional food preparation methods (which they prided themselves on)," on the other hand, the contract was fundamentally commercial in nature, and such contracts are "unlikely to satisfy the legal threshold" of warranting such damages. Giancaspro, *supra* note 2, at 89.

[38] *Id.* at 90.

[39] Such cases are discussed by Dr. Giancaspro in *id.* at 91.

[40] Such as the "casket" cases. *See, e.g.*, FARNSWORTH, *supra* note 24, § 12.17, 810; *see also* RESTATEMENT (SECOND) OF CONTRACTS § 353 (Damages for mental distress are generally only available if "the contract or the breach is of such a kind that serious emotional disturbance was a particularly likely result.").

[41] *See* Giancaspro, *supra* note 2, at 92–96.

[42] *See id.* at 92–93.

[43] *See, e.g.*, RESTATEMENT (SECOND) OF CONTRACTS § 351 ("Damages are not recoverable for loss that the party in breach did not have reason to foresee as a probable result of the breach when the contract was made."); Hadley v. Baxendale, 156 Eng. Rep. 145, 151 (1854) ("Where two parties have made a contract which one of them has broken, the damages which the other party ought to receive in respect of such breach of contract should be such as may fairly and reasonably be considered either arising naturally, i.e., according to the usual course of things, from such breach of contract itself, or such as may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it.").

certainly be rejected by U.S. courts, which have long denied punitive damages in contract law outside of a few well-recognized exceptions.[44]

IV. ANALYSIS AND CRITIQUE

As Dr. Giancaspro points out, even if the McDonald brothers succeeded on any of the claims discussed above, their contract "damages" would probably be completely absorbed by the increased profits they pocketed as a result of Mr. Kroc's (financially) advantageous breach.[45] But is this right? Has not the defendant, after all, committed a wrong, and an egregious one at that? And, if so, should the defendant be allowed to escape paying damages for these wrongs because he got "lucky" that the breach turned out to be so profitable to the plaintiffs?

Although he did not state the question in quite this way, Dr. Giancaspro agrees with some of the older English decisions on the point, which held that "a plaintiff should not have their damages reduced where the benefits that flowed to them following the defendant's breach were not anticipated nor wanted."[46] Dr. Giancaspro goes on to explain that "[i]t would seem just in the circumstances not to penalize the plaintiffs in situations where they had no reasonable opportunity to attempt mitigation,"[47] and this intuitively makes sense to me.

But why? According to Dr. Giancaspro, this principle is "both commercially sensible and innately just" and "reflects the law's disdain for parties who wrongfully undermine the cooperative nature of contractual relations."[48] Here, I could hardly agree more, and have recently written about how courts, under the guise of "compensation," frequently do "punish" parties (without ever using those words) through more generous compensatory damages awards and by reducing the effectiveness of a defendant's arguments to limit such damages where the defendant's behavior was particularly blameworthy.[49] As such, the spirit informing the solution favored by Dr. Giancaspro seems to apply to situations that go far beyond those resulting in an "advantageous breach" to the promisee—and the key, I think, is to

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[44] *See id.* at 761–62 (discussing punitive damages where the contract breach is also tortious, where the breach is accompanied by an independent tort, where the promisor's conduct was "fraudulent," and where insurers have refused to settle insurance claims in bad faith).

[45] *See* Giancaspro, *supra* note 2, at 101–02.

[46] *See id.* at 104; *see also id.* at 106 ("Where the plaintiff takes no mitigatory steps either as a consequence of lack of knowledge of the defendant's breach, or due to the defendant's prevention of the plaintiff taking such steps, and the plaintiff still enjoys benefits arising directly from the defendant's breach, those benefits should not be regarded as avoided losses nor offset against the plaintiff's losses.").

[47] *Id.* at 104.

[48] *Id.* at 106.

[49] *See generally* Marco Jimenez, *Retribution in Contract Law*, 52 UC DAVIS L. REV. 637 (2018).

explain exactly why this might be so. This is just a hunch, but I suspect the answer lies, at least in part, on the nature of the wrong that was committed when the promisor breached,[50] which is a completely separate issue from the "damages" that just so happened to arise (or not) from that breach. Damages, after all, do not exist in a vacuum, and are meant not only (or, more controversially, even primarily) to compensate victims of breach, but to vindicate the very rights that were transgressed by the breach.

Yet another avenue that Dr. Giancaspro could have pursued in his article would be a potential claim for disgorgement by the McDonald brothers under the recent Restatement (Third) of Restitution and Unjust Enrichment § 39.[51] According to this provision, the brothers might have been more successful by focusing not on their losses, which is the primary focus of Dr. Giancaspro's article, but rather on Mr. Kroc's gains. Specifically, the brothers could be entitled to "the profit realized by the promisor as a result of the breach[,]" if they could prove that (1) Mr. Kroc's breach was deliberate, (2) profitable, and that (3) the available damage remedy would insufficiently protect the McDonald brothers' contractual entitlement (yes, yes, and

[50] For example, one might wish to consider the following: How intentional was the breach? How blameworthy was the promisor's conduct? How vulnerable was the promisee? What were the circumstances under which the beach was committed? *See generally id.*
[51] Specifically, the Restatement (Third) of Restitution and Unjust Enrichment provides as follows:

> § 39. Profit From Opportunistic Breach
>
> (1) If a deliberate breach of contract results in profit to the defaulting promisor and the available damage remedy affords inadequate protection to the promisee's contractual entitlement, the promisee has a claim to restitution of the profit realized by the promisor as a result of the breach. Restitution by the rule of this section is an alternative to a remedy in damages.
>
> (2) A case in which damages afford inadequate protection to the promisee's contractual entitlement is ordinarily one in which damages will not permit the promisee to acquire a full equivalent to the promised performance in a substitute transaction.
>
> (3) Breach of contract is profitable when it results in gains to the defendant (net of potential liability in damages) greater than the defendant would have realized from performance of the contract. Profits from breach include saved expenditure and consequential gains that the defendant would not have realized but for the breach, as measured by the rules that apply in other cases of disgorgement (§ 51(5)).

RESTATEMENT (THIRD) OF RESTITUTION AND UNJUST ENRICHMENT § 39 (AM. LAW INST. 2011).

yes).[52] Admittedly, the Restatement (Third) of Restitution and Unjust Enrichment was only published in 2011, and this rather novel "disgorgement" remedy would hardly have been available to them. However, a modern promisee who finds herself in the position of the McDonald brothers would certainly want to consider focusing not only on her losses, but on the promisor's gains as well.

V. CONCLUSION

These small points aside, Dr. Giancaspro has written an important and enjoyable article that discusses many of the most important claims likely to be made by the McDonald brothers against Mr. Kroc (even today), and, as such, should prove of value to anyone interested in figuring out how to give a meaningful remedy to a promisee where a promisor's breach has actually benefited the promisee whose rights have been infringed. I am likely to draw on this article in both my contracts and remedies classes in the future, and highly recommend it.

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[52] *Id.*