Fiduciary Duties

Directors and Employees

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desire to award the 'just' remedy on the given facts irrespective of the common law or equitable source of the obligation breached. Such a development is welcome.

1.14 Accessory liability in equity – whether it be dishonest assistance or knowing receipt – depends in part upon proving what was known to the assistant or recipient. The separate legal personality of a company means that if liability as an accessory is to be visited upon a company, knowledge must be attributed or imputed to it. Questions of knowledge, attribution and imputation also have an important role to play in the law on bribery on both sides of the transaction – did the briber have the requisite knowledge; did the recipient of the bribe disclose the bribe to his principal?

1.15 Perhaps the most complicated chapter concerns remedies, a topic with the capacity to generate confusion as well as controversy. The law has been clarified since the first edition but difficulties remain. Case law evidencing the way in which accounts and accounts of profits are fashioned is scant. Uncertainty breeds settlement. We have attempted to provide a coherent and principled analysis but are acutely conscious that the law is developing.

1.16 We have thought it useful to examine the impact of time limits on the pursuit of claims for breach of fiduciary duty and accessory liability. The Supreme Court has clarified the law in this area. This chapter is, of course, closely focused on the Limitation Act 1980 and thus has not required us to consider any comparative law.

1.17 In most of the other chapters, we have made use of Commonwealth case law, particularly that deriving from Australia and New Zealand. Canadian courts have provided us with less material because their approach to some of the issues differs significantly from that of English courts. Even with Australia and New Zealand, however, it has been necessary to tread carefully since there are some differences of substance – for example, the Australian High Court has not followed *Royal Brunei Airlines v Tan*[3] and has recently affirmed its continuing adherence to the rule as originally formulated in *Barnes v Addy*[4] and its approach to employee fiduciary obligations does not conform to the approach in this jurisdiction (at least not consistently).

[3] [1995] 2 AC 378.
[4] (1874) LR 9 Ch App 244.

CHAPTER 2

FIDUCIARY DUTIES

INTRODUCTION

Overview

> 'To say that a man is a fiduciary only begins the analysis; it gives direction to further inquiry. To whom is he a fiduciary? What obligations does he owe as a fiduciary? In what respect has he failed to discharge these obligations? And what are the consequences of his deviation from duty?'[1]

2.1 Directors undoubtedly owe fiduciary duties to the company in which they hold office. However, whilst this proposition is uncontroversial, across the common law world there have been divergent views as to what duties rank as fiduciary in their nature. The core directors' duties have been codified in the Companies Act 2006. All but the duty of skill and care under s 174 are to be regarded as fiduciary duties.[2]

2.2 In the context of employees the Court of Appeal decision in *Customer Systems plc v Ranson*[3] has provided welcome clarification that, where allegations that an employee is a fiduciary are made, the nature and scope of his duties are not safely to be analysed by reference to directors' duties.

2.3 What remains unsettled is the extent to which the principles underlying directors' duties (albeit not the duties themselves) are to be applied to employees. Notwithstanding the volume of academic writing and judicial consideration of fiduciary duties, there remains no settled definition or test for a fiduciary and no universal guide as to which duties apply, or their content, even if the conclusion is reached that a person is in a fiduciary relationship.

Summary of the current law concerning directors' and employees' fiduciary duties

2.4 We summarise the present state of English law on the nature and content of directors' and employees' fiduciary duties in the following propositions.

[1] Per Frankfurter J in *S.E.C. v Chenery Corporation* (1943) 318 US 80, at pp 85–86.
[2] Companies Act 2006 s 178(2); *Maidment v Attwood* [2012] EWCA Civ 998, [2013] Bus LR 753 per Arden LJ at para 22.
[3] [2012] EWCA Civ 841, [2012] IRLR 769.

(1) The word 'fiduciary' has been described as 'manifestly unstable'.[4] It is an etymological chameleon, used in different ways in different contexts:
   (a) as a noun, to connote an individual whose status is regarded as 'fiduciary' because of the position he holds; the paradigm example is the express trustee; the company director is another. Agents are commonly described as 'fiduciaries';
   (b) as an adjective;
      (i) to describe different equitable relationships:[5] influence, confidentiality and trust and confidence (of which the distinguishing feature is loyalty) have been identified as distinc fiduciary relationships.[6] It is the relationship of trust and confidence which is the focus of this work. Certain relationships are universally regarded as falling within this category: trustee/beneficiary; director/company; partners; solicitor/client;
      (ii) to describe the different duties owed by 'fiduciaries' within the various recognised relationships of trust and confidence eg trustees, directors, agents, partners, solicitors;[7]
      (iii) to describe the core directors duties codified at ss 171–173 and 175–177 of the Companies Act 2006;[8]
      (iv) in contradistinction to (ii) and (iii) above, to describe only those duties which exact undivided loyalty, which are peculiar to all fiduciaries and the breach of which attracts remedies peculiar to fiduciaries;[9]
      (v) Used forensically (and wrongly), of contractual or other duties in the hope of elevating those duties to the status of fiduciary duties so as to engage a more appealing remedial regime.[10]

(2) In response to a perceived lack of clarity of usage of the term 'fiduciary duty' the Court of Appeal in *Bristol & West Building Society v Mothew*[11] emphasised the need to limit such use to those particular duties of loyalty which are peculiar to fiduciaries, and which attract peculiar (restorative and restitutionary) remedies. It made clear that the duty to exercise skill and care was not a peculiarly fiduciary duty, because the duty was not concerned with the concept of loyalty, but with competence. Mere incompetence did not connote disloyalty.

(3) The decision in *Bristol & West* is widely cited as an authorative modern statement of the law. However, as regards the duties which are fiduciary it has not been consistently interpreted, whether by judges or academics. The

4 Birks 'The Content of Fiduciary Obligation' [2002] 16 TLI 34.
5 *Re Coomber: Coomber v Coomber* [1911] 1 Ch 723.
6 Sir Peter Millett 'Equity's Place in the Law of Commerce' (1998) 14 LQR 214.
7 Lord Browne-Wilkinson in *Henderson v Merrett* [1995] 2 AC 145 at 206B; see for a wide-spread description of other directors' duties as fiduciary sub-para (7) and footnote below.
8 Section 178(2) Companies Act 2006 and *Maidment v Attwood* [2012] EWCA Civ 998 para 22.
9 *Bristol & West Building Society v Mothew* [1998] Ch 1.
10 *Re Goldcorp Exchange* [1995] 1 AC 74; *Macquarie Internationale Investments Ltd v Glen (UK) Ltd* [2008] EWHC 1716 (Comm), [2008] All ER (D) 275.
11 [1998] Ch 1.

ambiguity has arisen from the statement that fiduciaries owe a 'duty of good faith'. This statement has been interpreted:
   (a) restrictively, as being limited to the no conflict and no profit duties;[12]
   (b) more broadly, as including a duty to act in good faith in the best interests of the company and embracing positive action on its behalf.[13]

(4) It is settled that English law recognises the 'no conflict' and 'no profit' rules as fiduciary duties. Such duties are peculiar to fiduciaries. They are codified in ss 175–176 of the Companies Act 2006.[14] The law on directors' duties has consistently recognised the 'proper purposes' duty[15] and the duty to act in good faith in the best interests of the company[16] as fiduciary duties.[17]

(5) The Companies Act 2006 has codified the general duties of directors which have effect in place of the common law rules and equitable principles upon which they are based.[18] Sections 171, 172, 173, 175, 176 and 177 are regarded as fiduciary duties,[19] although not each of those duties is 'peculiarly fiduciary'[20] as understood in *Mothew*.

(6) Although employees owe contractual duties of fidelity, the relationship between employee and employer is not inherently fiduciary. Fiduciary relationships may arise within the employment relationship where the role performed by the employee or particular tasks undertaken by him results in the imposition of fiduciary obligations.[21]

(7) The nature and content of employees' fiduciary obligations are not settled. Employees have not, traditionally, been regarded as owing a fiduciary duty in the terms of s 172 of the Companies Act 2006, and have never been held to owe a duty in the terms of s 171 of the Companies Act 2006 even where it has been held that they owe fiduciary duties.

12 See 2.72–2.87.
13 See 2.140 and following.
14 Together with other provisions concerning disclosure, consent and authorisation which support and qualify the rules: see ss 177, 180, 182, 183, 185, 187 and Chapter 4.
15 *Howard Smith Ltd v Ampol Petroleum Limited and others* [1974] AC 821.
16 *Re Smith and Fawcett Limited* [1942] 1 Ch 304.
17 For recent examples consider: *Extrasure Travel Insurance Ltd v Scattergood* [2003] 1 BCLC 598; *Ultraframe (UK) Limited v Fielding* [2005] EWHC 1638 (Ch); *Simtel Communications Ltd v Rebah & others* [2006] 2 BCLC 571; *Primlake Ltd (in liquidation) v Matthews Associates & others* [2007[1 BCLC 666; *Reeves v Sprecher* [2007] 2 BCLC 614; *Green v Walkling* [2007] EWHC 3251 (Ch); *Williams v Farrow & another* [2008] All ER (D) 328 (Feb); *Key-TV v Ramsay & another* [2008] All ER (D) 323 (Feb). See *Sinclair v Versailles* [2011], [2011] EWCA Civ 347, [2012] Ch 453, [2011] 3 WLR 1153, [2011] 4 All ER 335, [2011] Bus LR 1126, [2011] 2 BCLC 501; *Maidment v Attwood* [2012] EWCA Civ 998, [2013] Bus LR 753 per Arden LJ at para 22.
18 Section 170(3).
19 Section 178(2) of the Companies Act 2006 implies that all duties other than that of skill and care are fiduciary: 'The duties in [sections 171–173, 175–177] are, accordingly, enforceable in the same way as any other fiduciary duty owed to a company by its directors'. This status was confirmed by Arden LJ in *Maidment v Attwood* [2012] EWCA Civ 998 [2013] Bus LR 753 at para 22.
20 In the sense of giving rise to remedies peculiar to fiduciaries.
21 See Chapter 3.

(8) It is established that the duty of a director under s 172 CA 2006 may require him to disclose his own wrongdoing and information of interest to the company.[22] Such an approach has also been adopted in the case of employees,[23] with the effect that prescriptive duties are now being imposed on employees which are additional to the contractual obligations owed by them.[24]

(9) Fiduciary duties are not 'one size fits all'. Different types of relationship will apparently generate different duties with different content and application.[25] It is dangerous to reason by analogy from cases about company directors to cases about employees.[26]

General duties under the 2006 Companies Act

2.5 The general duties owed by directors are set out in ss 171–177 of the Companies Act 2006. More than one of the general duties may apply in any given case.[27] We summarise them below.

(1) Section 170 is an introductory section. It identifies the scope and nature of the general duties, and, significantly provides that they 'have effect in place of' those common law rules and equitable principles upon which they are based.[28]

(2) Section 171 sets out the duty to act within powers, imposing a duty requirement that the director act within the constitution and for proper purposes.[29]

(3) Section 172 sets out the duty to promote the success of the company in the way the director considers, in good faith, would be most likely to promote the success of the company for the benefits of its members.[30]

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22 *Item Software (UK) Ltd v Fassihi* [2005] 2 BCLC 91.

23 *Hanco ATM Systems Ltd v Cashbox ATM Systems Ltd & others* [2007] EWHC 1599 (Ch), [2007] All ER (D) 139 (Jul); *Governor of the Bank of Ireland v Jaffery* [2012] EWHC 1377 (Ch) and *QBE Management Services Ltd v Dymoke* [2012] EWHC 80 (QB).

24 This approach is controversial. Attempted imposition of such fiduciary obligations on directors and employees has been rejected in Australia: *P&V Industries v Porto* (2006) 14 VR 1.

25 See *Customers Systems plc v Ranson* [2012] IRLR 769; *F&C Investment LLP v Barthelemy*; *Ross River v Waveley*. Note also that in its Consultation Paper and Report on Fiduciary Duties and Regulatory Rules No 124 1995 the Law Commission concluded that there were two proscriptive, prophylactic duties: 'no conflict', 'no profit' and 'undivided loyalty' (the 'no conflict' of duty and duty) and a duty not to misuse confidential information. By contrast, in *Report into the Reform of Directors Duties*, the Company Law Reform Steering Group categorised as 'fiduciary duties' all of the duties which are now described as 'fiduciary' in the codified general duties *Modern Company Law for a Competitive Economy* URN 01/942 Section B11 paras 11.4–11.20.

26 See *Customer Systems plc v Ranson* [2012] EWCA Civ 841, [2012] IRLR 769.

27 Companies Act 2006, s 179.

28 Companies Act 2006, s 170(3).

29 See *Howard Smith Ltd v Ampol Petroleum and others* [1974] AC 821.

30 *In re Smith and Fawcett Ltd* [1942] 1 Ch 304. *Regentcrest plc (in liq) v Cohen* [2001] 2 BCLC 80.

(4) Section 173 contains a duty to exercise independent judgment. It is thought that this reflects the law precluding a director from fettering his discretion.[31] It also appears to reflect the obligation on a director not to abrogate personal responsibility.[32]

(5) Section 174 contains the duty to exercise reasonable skill and care, and adopts the approach of s 214 of the Insolvency Act 1986 as to the standard required.[33]

(6) Section 175 provides that a director must avoid situations of conflict of interest: including conflict between his duty to the company and his personal interest,[34] and between his duty to the company and his duty to a third party.[35]

(7) Section 176 precludes a director from accepting benefits from third parties conferred by reason of his position or actions as a director.[36]

(8) Section 177 imposes a duty to declare an interest in proposed transactions or arrangements.[37]

Continuing relevance of fiduciary duties

2.6 Despite the intervention of statute, the general law remains important.

(1) Although the general duties of directors stipulated by the Act have effect in place of the common law rules and equitable principles upon which they are based,[38] they are to be interpreted and applied in the same way as the common law rules or equitable principles which they replace and 'regard shall be had' to those rules and principles for that purpose.[39] Therefore, existing case law will fashion the interpretation of the general duties.

(2) Secondly, s 178(1) of the Act provides that:

> '(1) The consequences of breach (or threatened breach) of ss 171 to 177 are the same as would apply if the corresponding common law rule or equitable principle applied.'

Therefore, the availability of any remedy will depend upon the proper characterisation of both duty and breach. This is of particular importance

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31 *Fulham Football Club Ltd v Cabra Estates plc* [1992] BCC 863.

32 Eg *Re Simmon Box (Diamonds) Ltd* [2000] BCC 275.

33 As adopted in *Norman v Theodore Goddard* [1991] BCLC 1028; *Re D'Jan of London Ltd* [1993] BCC 646.

34 The 'no conflict' rule: *Aberdeen Railway Co v Blaikie* (1854) 1 Mac 1 461 which also embraces the no profit rule.

35 As extended following *Transvaal Lands Company v New Belgium (Transvaal) Land and Development Company* [1914] 2 Ch 488.

36 (In part) the 'no profit' rule: *Regal (Hastings) Ltd v Gulliver* [1967] 2 AC 134, as applied to secret commissions and bribes.

37 Together with ss 182, 183, 185 and 187 these sections replace (with modifications) Companies Act 1985, s 317.

38 Section 170(3).

39 Section 170(4).

where breaches of fiduciary duty may give rise to proprietary a accounting remedies which do not otherwise arise.

(3) Fiduciary regulation will continue to develop through case-law in oth fields. Decisions by the courts upon the interpretation of fiduciary du under the Act will be exported and applied to other fiduciary relationsh and vice versa. This is expressly recognised in the Explanatory N which accompany the Act. They state that:[40]

> '[i]n the company law field, the principles being applied will frequentl taken from other areas, in particular trusts and agency. It is important t these connections are not lost and that company law may continue to r developments elsewhere. Frequently the courts may formulate the same in different ways. In contrast, legislation is formal. It is not easy to reco these two approaches, but the sections seek to balance precision against need for continued flexibility and development.'

There are notable features of the new duties as codified which reveal a cha of emphasis from the common law position; for example: the factors which are to be considered by a director under s 172, the terms of s 173, the yoking of the no profit rule to the no conflict rule in s 175, and the formal abandonment of the prohibition on self-dealing in favour of a statutory disclosure obligation under s 178 and related provisions. However, little controversy has emerged to date, and the general assumption (perhaps to the dismay of those involved in the passage of the Act through Parliament) has been that the previous law remains largely unchanged.[41]

THE FIDUCIARY PRINCIPLE

2.7 In this section we explore what is meant by the term 'fiduciary' in the context of duties owed by directors and employees.

Three fiduciary doctrines?

2.8 Writing extra-judicially Sir Peter Millett identified three distinct categories of fiduciary relationship:

(1) trust and confidence (the defining characteristic of which was said to be loyalty);
(2) undue influence (the defining characteristic of which is vulnerability); and
(3) confidentiality (whenever information is imparted by one person to another in confidence).[42]

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40 Paragraph 305.
41 See eg *Towers v Premier Waste* [2011] EWCA Civ 923, [2012] BCC 72; *Thermascan Norman* [2009] EWHC 3694 (Ch), [2011] BCC 535; *Sharma v Sharma* [2013] EWCA Civ 1287, [2014] BCC 73, cf *Killen v Horseworld* [2012] EHC 363 (QB).
42 'Equity's Place in the Law of Commerce' (1998) 14 LQR 214.

2.9 There is academic and judicial debate as to the extent to which, in modern times, undue influence and confidentiality are properly to be regarded as 'fiduciary' doctrines.[43] We do not engage in that debate. We consider, separately, the obligations of confidentiality in the context of directors and employees in Chapter 5. We do not consider the doctrine of undue influence in this work.[44]

The relationship of trust and confidence: loyalty

2.10 The duties considered in this chapter arise from the first category of relationship identified by Sir Peter Millett, namely that of trust and confidence, the defining characteristic of which is loyalty. The focus is upon an analysis of those duties which are peculiar to fiduciaries and the breach of which attracts those different legal consequences to which Millett LJ referred in *Bristol & West Building Society v Mothew*.[45] We do so because, in an area of law which has historically defied definition and categorisation, this provides a widely accepted foundation for analysis.

Duties peculiar to fiduciaries

2.11 In *Bristol & West Building Society v Mothew*[46] Millett LJ had to consider the claimant's contention that solicitors who had acted for it in a property conveyance had acted in breach of fiduciary duty. In a celebrated passage, he held as follows:[47]

> 'Despite the warning given by Fletcher Moulton LJ in *Re Coomber: Coomber v Coomber*[48] this branch of the law has been bedevilled by unthinking resort to verbal formulae. It is therefore necessary to begin by defining one's terms. The expression 'fiduciary duty' is properly confined to those duties which are peculiar to fiduciaries and the breach of which attracts legal consequences differing from those consequent upon the breach of other duties. Unless the expression is so limited, it is lacking in practical utility. In this sense it is obvious that not every breach of duty by a fiduciary is a breach of fiduciary duty.'

2.12 Although this was a solicitor's case, its reasoning has been adopted as being applicable to directors.[49] Further, Millett LJ's statement that the duty to

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43 See eg *Arklow Investments v Maclean* [2000] 1 WLR 594; *Nottingham University v Fishel* [2000] ICR 1462 at p 1489 referring to the three categories of fiduciary relationship adumbrated by Sir Peter Millett in 'Equity's Place in the Law of Commerce' (1998) 14 LQR 214. In *Generics (UK) Ltd v Yeda Research & Development Co Ltd* [2012] EWCA Civ 726 Etherton LJ analyses duty of confidentiality by reference to the 'fiduciary' doctrine.
44 Although we consider below the relevance of the historic recognition of this tri-partite categorisation.
45 [1998] Ch 1.
46 [1998] Ch 1 at p 17.
47 Approved by the House of Lords in *Hilton v Barker Booth & Eastwood* [2005] 1 WLR 567 at 575 para 28.
48 [1911] 1 Ch 723 at 728.
49 *Gwembe Valley Holdings v Koshy* [2004] 1 BCLC 154, CA; *Ultraframe (UK) Ltd v Fielding*

CHAPTER 3

EMPLOYEES OWING FIDUCIARY DUTIES

INTRODUCTION

Scope of chapter

3.1 In Chapter 2 we explored the concepts underlying fiduciary loyalty and the current state of the law in this area. In this chapter we turn the spotlight on the law's approach to identifying fiduciary relationships in the context of the employment relationships.

3.2 In *Phipps v Boardman*[1] Lord Upjohn set out a four-part test to identify the existence and scope of a fiduciary relationship.

(1) First one has to examine the facts and circumstances to see whether the individual (whatever label is applied to describe him, eg agent) is in a fiduciary relationship to his principal.

(2) Once such a relationship is established, it must be examined to see what duties are imposed on the individual, to see what is the scope and ambit of the duties imposed on him.

(3) Having defined the scope of the duties, one must see whether the individual has committed a breach and 'by placing himself within the scope and ambit of those duties in a position where his duty and interest may possibly conflict. It is only at this stage that any question of accountability arises.'

(4) An individual is only accountable for profits made within the scope and ambit of his duty.

The aim of this chapter is to provide a framework within which to answer the above test in the context of the employment relationship.

3.3 The modern approach under English law is that the employee/employer relationship is not a fiduciary relationship, but that a fiduciary relationship between employer and employee may arise from the terms of the employment contract where particular contractual obligations require an employee to act solely in the employer's interest. The leading case in this area is the decision of

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[1] [1967] 2 AC 46 at p 127. Lord Upjohn dissented in the result, but this approach has since been followed: see eg *IDC Ltd v Cooley* [1972] 1 WLR 443.

Elias J in *University of Nottingham v Fishel*.[2] It has now been authoritatively approved by the Court of Appeal.[3] In this chapter we identify the concepts underlying the fiduciary doctrine as it applies to employees, summarise the approaches adopted in earlier case law and in commonwealth authority, which continue to inform the development of English law, provide an analysis of the decision in *Fishel* and its application in subsequent cases, and give practical consideration to the types of roles and duties which will give rise to fiduciary duties being owed by employees.

Background to claims against employees for breach of fiduciary duty

3.4 The incidence of claims against employees for breach of fiduciary duty has increased sharply in recent years. Why is this? We venture five reasons.[4]

3.5 First, 'Mammon' remains 'an insidious subverter'.[5] The rationale underlying the imposition in equity of the duties discussed in Chapter 2 remains as relevant today as it did in 1726 when *Keech v Sandford* was decided.[6] An expanding and sophisticated global services industry with enormous financial rewards, in particular in the financial sector, for those who succeed, has done nothing to deter employees who seek to advance their private interests at the expense of their employers. As Lord Millett observed, writing extra-judicially in *Equity's Place in the Law of Commerce*:[7]

> 'Equity exacts higher standards than those of the market place, where the end justifies the means and the old virtues of loyalty, fidelity and responsibility are admired less than the idols of "success, self-interest, wealth, winning and not getting caught".[8] It is unrealistic to expect that employees can be given incentives through enormous bonuses without undermining their business ethics.'

3.6 We would observe that in a market-place which is increasingly driven by incentives, be they by way of commission, employee share plans or stock options, the risk of 'loyalty, fidelity and responsibility' being compromised increases correspondingly. Substantial contractual incentives may be thought to enhance the likelihood that the employer's interests will be promoted to the greatest extent possible by the employee. However, they place temptation in the path of unscrupulous employees to cut corners, massage order books and inflate figures.

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2 [2000] ICR 1462.
3 *Helmet Integrated Systems Ltd v Tunnard* [2007] IRLR 126, [2007] FSR 16; *Customs Systems plc v Ranson* [2012] EWCA Civ 841.
4 And acknowledge the influence of Sir Peter Millett's article 'Equity's Place in the Law of Commerce' [1998] 114 LQR 214.
5 Elias J in *University of Nottingham v Fishel* [2000] ICR 1462 at p 1475A.
6 (1726) Sel Cas t King 61, (1726) 25 ER 223.
7 (1998) 114 LQR 214 at p 216.
8 Sacks *The Politics of Hope* (1997) p 179.

3.7 Secondly, advances in technology, in particular text, email and the internet and more recently wider social media, have resulted in more employees 'getting caught'. Employers can discover a great deal more about a careless employee's supposedly private activities than was historically the case through scrutiny of social media, interrogation of email and through electronic and other searches which can uncover information about newly formed companies and their activities.

3.8 Thirdly the traditional 'master/servant' employment model had had its day. As the UK service industry has developed to replace a declining industrial workforce, employment structures are changing. A traditional 'manual' or 'blue-collar' workforce is rare. The present employment climate recognises that an employee's status is prized, although long-term employment is increasingly unusual in the private sector. Many large companies will employ tiers of employees in management positions, often with the title 'director', confer considerable responsibility on them, and pay them commensurately, but will not appoint them as statutory directors. Substantial authority is vested in them to conduct their employer's affairs on the company's behalf or at the least to exercise substantial influence over how those affairs are conducted. In smaller companies with limited resources even junior employees may have delegated authority to carry out some part of the company's business on its behalf without ever being appointed a director or even being considered a senior employee.[9]

3.9 Fourthly, the law of equity governing accessory liability (which we consider in Chapter 7) has developed teeth and currency in recent times, and affords possible attractive[10] remedies against third parties who have knowingly lent themselves to a breach of duty by a fiduciary. The employee's breach of duty will not necessarily result in any substantial personal benefit. An employee cannot be required to account for profits which he has not made.[11] Even if the breach does result in personal benefit to the employee, the proceeds may have been dissipated by the time the employer is aware of his right to claim. The profit may be made by accessory third parties. However, irrespective of the conduct and guilty mind of the accessory, no claim can be made to such profits unless the claimant employer establishes that the relevant employee owed him, and acted in breach of, a fiduciary duty.[12]

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9 In our view a nebulous and unhelpful description by which to assess whether fiduciary duties are owed.
10 In the case of dishonest assistance in a breach of fiduciary duty the law is not necessarily settled as to what remedies are available: see 9.292–9.332.
11 See Chapter 9 below.
12 The approach of the House of Lords *Attorney-General v Blake* [2001] 1 AC 268 in which the remedy of an account of profits was awarded for breach of contract was for a time largely regarded as confined to its exceptional facts. It has still not gained currency, although the climate for such an award, and awards of 'restitutionary damages' is becoming more favourable: see Chapters 4 and 9.

3.10 Finally, there is a growing awareness amongst employment practitioners of a potential lifeline leading to a worthwhile remedy in equity where their clients have suffered no loss. In *Equity's Place in the Law of Commerce* Lord Millett wrote as follows:

> '... [Claimants] and their advisers have discovered the apparent advantages of alleging breach of trust or fiduciary duty, with the result that a [Particulars] of Claim is considered to be seriously deficient if it does not contain inappropriate references to these concepts which are often scattered throughout the pleadings with complete abandon.'

The courts, however, are becoming wise to attempts by lawyers to clothe common law claims for breach of contract or negligence in equity's garb in such circumstances.

3.11 In *Attorney-General v Blake*[13] the Court of Appeal adopted Sopinka J's salutary warning in the decision of the Canadian Supreme Court in *Norberg v Wynrib*[14] that 'fiduciary duties should not be superimposed on those common law duties simply to improve the nature or extent of the remedy'.

CONCEPTS UNDERLYING THE FIDUCIARY DOCTRINE

3.12 We deal in greater detail with concepts underlying the fiduciary doctrine in Chapter 2 and in relation to remedies in Chapter 9. However, we set out below a summary of the main elements.

Loyalty, influence and confidentiality

3.13 In his article *Equity's Place in the Law of Commerce*[15] Lord Millett identified three distinct but intertwined fiduciary relationships.[16] Of these the most important was the relationship of trust and confidence, of which the core obligation was loyalty. It is this relationship with which this book is principally concerned, and which gives rise to the fiduciary duties discussed in Chapter 2 and summarised below.

3.14 The other two categories of relationship identified by Lord Millett are 'influence' of which the distinguishing feature was said to be vulnerability and 'confidentiality' which arises whenever information is imparted by one person to another in confidence. We consider confidentiality in Chapter 5. It is controversial whether the relationships of influence and confidentiality are truly 'fiduciary'. That is not a controversy which it is necessary to resolve in this

13 [1998] Ch 439.
14 (1992) 92 DLR (4th) 449 at 481.
15 (1998) 114 LQR 214.
16 The other two being 'influence' and 'confidentiality' – at pp 219–220.

work. We note briefly these two other relationships, however, because of the importance of understanding and keeping distinct the different sources of equitable obligations.[17]

3.15 Employees will frequently be privy to confidential information imparted in the course of the employment relationship. This does not, of itself connote, that an employee will owe the fiduciary duties which stem from the separate relationship of trust and confidence. The Court of Appeal in *Attorney-General v Blake*[18] issued a stern warning against attaching to one type of relationship (eg confidentiality) an obligation which is properly derived from another (eg trust and confidence):[19]

> 'The two relationships are not mutually exclusive. They may co-exist between the same parties at the same time. But they generate different obligations, and their duration may be different.'

3.16 Nevertheless, as we explore below, the three equitable relationships are closely linked. Concepts of 'influence' and 'vulnerability' have influenced judges in determining whether an employee owes fiduciary duties of undivided loyalty to his employer.[20] Lord Millett himself recognised that the duties 'intertwined'.[21]

Who is a fiduciary?

3.17 Judges and jurists have been unwilling to formulate any universally accepted definition of a fiduciary. The concept has its modern origin in the law of trusts.[22] A fiduciary can therefore be regarded as someone whom one can trust and rely on.[23] However, that is too broad a concept to be useful to lawyers seeking to understand what distinguishes fiduciary duties from other duties owed under contract, in tort, under statute or generally in equity. A fiduciary is someone who has undertaken to, or is obliged to, act in the interests of another. He is required to demonstrate single-minded loyalty to his principal.[24] Loyalty in this context has a particular meaning, namely the avoidance of self-interest. Fiduciaries are obliged to avoid self-interest in their dealings with their principals.[25]

17 *Re Coomber: Coomber v Coomber* [1911] 1 Ch 723 at pp 728–729.
18 [1998] Ch 439.
19 At p 454H. See *Generics (UK) Ltd v Yeda Research & Development Co Ltd* [2012] EWCA Civ 726 per Etherton LJ at para 76.
20 See eg Moses LJ in *Helmet Integrated Systems Ltd v Tunnard* [2007] IRLR 126, [2007] FSR 16 at para 45 in which he identified vulnerability as the defining characteristic of the relationship of trust and confidence. Lord Millett had, however, identified it as the defining characteristic of the relationship of influence.
21 Page 221.
22 *Keech v Sandford* (1726) Sel Cas t King 61, (1726) 25 ER 223.
23 Birks 'The Content of Fiduciary Obligation' [2002] 16 TLI 34 at p 36.
24 *Bristol & West Building Society v Mothew* [1998] Ch 1.
25 See Chapter 2, 2.13–2.30.

What are fiduciary duties?

3.18 The content of the obligation of fiduciary loyalty is not settled. The negative formulation of 'avoidance of self-interest' in our description of the essence of what is required of a fiduciary, reflects the two core fiduciary duties which are negative in content. On one view, the content of fiduciary loyalty is limited to these two duties, and is thus purely proscriptive.[26] Such duties tell the fiduciary what he is not permitted to do.[27] They do not tell the fiduciary what he is required to do. In the case of an employee, the starting point is that what he is required to do is dictated by the express and implied terms of the contract of employment.

3.19 The two core negative duties are as follows:[28]

(1) The duty to avoid a situation in which an individual has, or can have, a direct or indirect interest that conflicts, or possibly may conflict, with the interests of his employer (the 'no conflict' duty);[29]

(2) The duty on an individual not, without authority, to make a profit directly or indirectly from the use of property subject to the fiduciary relationship or in the course of the fiduciary relationship and by reason of his fiduciary position.

3.20 The alternative, prescriptive view, would embrace, for example, a duty of good faith to act in the best interests of the employer; Such a duty has been held to impose obligations of disclosure on directors[30] and employees[31] to disclose personal wrongdoing and information of interest to the company/employer. The law is developing and is in a state of flux. We consider the competing authority and views in Chapter 2.

3.21 We consider, so far as employees are concerned, that if such positive prescriptive duties of disclosure are owed at all by employees to their employers, it is not (or should not be) as a result of the incursion of equity into the employment field, but as a result of the operation of the contract between

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26 Conaglen *Fiduciary Loyalty* (Hart, 2010).

27 *Attorney-General v Blake* [1998] Ch 439.

28 We have adopted the wording of ss 175 and 176 Companies Act 2006. They reflect common law. While those provisions will not be applied directly to employees, they are to be applied by analogy where an employee owes fiduciary duties to his employer.

29 The statutory definition under s 175 Companies Act 2006 includes conflicts between duty and interest and conflicting duties (s 175(7)). Although framed in terms of conflict between duty and interest, the duty has historically been recognised as applying solely to conflicts between duty and interest and duty and duty – see Chapter 2.

30 *Item Software (UK) Ltd v Fassihi* [2005] 2 BCLC 91.

31 *Hanco ATM Systems Ltd v Cashbox ATM Systems Ltd* [2007] EWHC 1599 (Ch), [2007] 4 ER (D) 139 (Jul) at para 65 following *Item Software (UK) Ltd v Fassihi*; *Tesco Stores Ltd v Pook* [2004] IRLR 618, applied in *Governor of the Bank of Ireland v Jaffery* [2012] EWHC 1377 (Ch).

the parties. We consider that this view is supported by the approach of the Court of Appeal in *Customer Systems plc v Ranson*,[32] for reasons analysed below and in Chapter 2.

3.22 The two negative duties overlap.[33] The Companies Act 2006 has codified these duties, as they apply to directors, in ss 175 and 176.[34] We have adopted the statutory terminology where appropriate. Although the statutory duties will not apply directly to non-director employees, they have been held to reflect the general law,[35] and it is not likely that employees will be held to a more stringent code of behaviour than directors. Section 176(4) of the Companies Act 2006 provides that there will be no breach of the 'no profit' duty 'if the acceptance of the benefit cannot reasonably be regarded as likely to give rise to a conflict of interest'. This clarifes that the rationale for the duty not to accept benefits is the risk of a conflict between duty and interest. As Sir Peter Millett has put it:[36] 'the second rule invites the question "why not?"; the first supplies the answer.'

Breach

3.23 Breaches of fiduciary duty may or may not be deliberate. They may result from the dishonest behaviour of an employee effectively defrauding his employer. They may, however, be 'attended with perfect good faith'[37] and without any intention on the part of the employee to defraud or otherwise harm the employer.[38] The mere fact of potential conflict between duty and interest or the making of an unauthorised profit where there is a risk of conflict is sufficient to trigger breach of duty.

3.24 The argument that proof of a potential conflict of interest did not suffice, and that an actual conflict of interest was necessary to bring home liability to an employee who was not a fiduciary per se, but only owed a fiduciary duty in limited respects, has been rejected at first instance.[39] The absence of a statutory

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32 [2012] EWCA Civ 841, [2012] IRLR 769; see further Frazer 'The employee's contractual duty of fidelity' (2015) LQR 131 Jan 53-77 in which he considers that English law regards fiduciary duties imposed on employees as being subsidiary and prophylactic and supportive of the employee's contractual duties: see p 72 citing Conaglen *Fiduciary Loyalty* (Hart, 2010) p 4.

33 *Chan v Zacharia* (1984) 154 CLR 178 per Deane J at pp 198–199 approved in *Don King Productions Inc v Warren* [2000] Ch 291 at 341 per Morritt LJ and *Ultraframe v Fielding* [2005] EWHC 1638 (Ch) at paras 1305–1306 and 1318. See further 2.93–2.98.

34 The 'no profit' rule is reflected in both s 175 and s 176 – see 2.89–2.91.

35 Generally – see Chapter 2, at 2.6 as to the narrowing of the 'no profit' duty under statute and *Towers v Premier Waste Management Ltd* [2011] EWCA Civ 923, [2012] BCC 72, [2012] 1 BCLC 67, [2012] IRLR 73.

36 'Bribes and Secret Commissions' [1993] RLR 7 at p 9.

37 Lord Herschell in *Bray v Ford* [1896] AC 44.

38 Although proof of intention will be required where the potential conflict is between duty to the employer and duty to a third party if fully informed consent has been obtained to the potential conflict – see the 'inhibition' principle – *Bristol & West Building Society v Mothew* [1998] Ch 1 at p 20.

39 *Airbus Operations Limited v Paul Withey & others* [2014] EWHC 1126 (QB) per HHJ Havelock-Allan QC at paras 129–130.

employer's interests. The risk of including such terms if the employee is junior and his pay is low, is that a court may declare them to be in (direct) restraint of trade.[262]

(4) Finally, and most importantly, attention should be given to defining the duties owed under the contract so as to emphasise the tasks and responsibilities owed by the employee. Caution is required, however, on two counts. First, where questions of a separate fiduciary relationship arise, the court is likely to be influenced by the substance of the relationship over its form. Secondly (and in particular so far as more junior employees are concerned), the more detailed the exposition of the duties in the contract and how they are to be performed, the more likely that a court will conclude that there is no need (or room) for the imposition of fiduciary duties.[263]

(5) It may well be, however, that many employers will prefer to provide in the contract for the necessary controls over (and careful supervision of) its employees' activities. This may preclude an equitable remedy, but may forestall the need to pursue a claim in the first place. In the light of the decision of the Court of Appeal in *Customer Systems plc v Ranson*[264] it would be advisable for any employer to provide expressly in respect of any reporting or disclosure duties.

262 But see 3.174 above.
263 See *Hospital Products v United States Surgical Corporation* [1984] 156 CLR 41.
264 [2012] EWCA Civ 841.

CHAPTER 4

CONTRACTUAL ISSUES

INTRODUCTION

4.1 In this chapter, we consider aspects of the contract of employment which may have a bearing on the tactical decision to be taken by an employer when it finds that an employee or ex-employee is embarking on a course of conduct which threatens the welfare of the employer's business. One option for the employer is to frame its allegations in contract. The other is to ascertain whether the employee owes fiduciary duties and base a claim on those equitable duties. The subject matter of this chapter is also considered so far as it impacts on the treatment of fiduciary duties, in context, in Chapters 2, 3 and 5.

4.2 Part of the employer's calculation when faced with a threat from an employee may reflect a perception that the contractual terms will not yield an effective injunctive remedy which might yet be available if the claim were formulated as a breach of fiduciary duty. Or the employer may consider that the contractual duties are narrower in scope than a fiduciary duty. Thirdly, the benefit of post-termination covenants may be thought to have been lost by reason of a repudiatory breach by the employer. Fourthly, there may be different and preferable remedies if the matter can be classified as a breach of fiduciary duty.

THE DUTY OF FIDELITY

4.3 As articulated by Lord Esher MR in *Robb v Green*[1] the duty of fidelity is '... a stipulation that the servant will act with good faith towards his master'.[2] It was a term which formed part of the contract of employment by 'necessary implication'. Some employees will also owe fiduciary duties. Nevertheless, it is important to acknowledge at the outset that, unlike the position of a director, the contemporary view is that '... the essence of the employment relationship is not typically fiduciary at all. Its purpose is not to place the employee in a position where he is obliged to pursue his employer's interests at the expense of his own.'[3] Elias J observed that 'care must be taken not automatically to equate the duties of good faith and loyalty ... with fiduciary obligations'.[4]

1 [1895] 2 QB 315.
2 See p 317.
3 Per Elias J in *Nottingham University v Fishel* [2000] ICR 1462 at 1491E.
4 See p 1493D.

4.4 Single-minded loyalty is the core liability of an individual who owes fiduciary duties. This requires such a person to subordinate his interests to those of his employer. By contrast, the contractual duty of fidelity does not of itself require that the employee should at all times act solely in the interests of his employer.

4.5 Nevertheless, although different in substantive content as the Court of Appeal noted in *Customer Systems plc v Ranson*,[5] loyalty is the concept which lies at the heart of both fiduciary duties and the duty of fidelity. Whilst fiduciary duties connote an obligation of undivided loyalty, Elias J's dictum suggests that, in relation to the duty of fidelity, divided loyalties are permissible in certain circumstances. A qualified or limited duty of loyalty may be easy to state but it is a rather difficult notion to understand. Undivided loyalty requires little by way of calibration. In any given circumstances, it is relatively simple to ascertain whether an individual has acted in a manner which reveals an absence of single-minded loyalty. By contrast, because the duty of fidelity has limits, it can be difficult to predict with confidence whether an employee's conduct has gone beyond those limits. This is especially the case when considering the acts which an employee may undertake preparatory to leaving and setting up in competition.

4.6 It may be difficult for an employee to balance his interests with those of his duty of loyalty. On the one hand, exploring alternative employment or even preparing to compete may be permissible. On the other hand, even defensive acts by an employee may breach the duty of fidelity if it involves the unauthorised use of the employer's information.[6]

Origins of the duty of fidelity

4.7 Fiduciary duties are imposed in equity whilst the duty of fidelity arises at common law as an implied term. This difference in origin might be thought to explain how it has come about that the two duties give rise to differing demands of loyalty. However, when one examines the jurisprudential origin of the duty of fidelity, it can be seen that the terms has roots in both the common law and equity.[7]

4.8 *Robb v Green*[8] is usually taken as the modern starting point when citing authority relating to the implied duty of fidelity. Mr Green secretly copied a list of names and addresses of customers with the intention of soliciting orders after his employment by the Plaintiff had come to an end. The claim was advanced as a contractual claim. Hawkins J found that there was an implied term that the defendant would not use, to the detriment of the employer, information to which he had access in the course of his service. The Court of Appeal upheld

5 [2012] EWCA Civ 841 [2012] IRLR 769.
6 Eg *Brandeaux Advisers (UK) Ltd v Chadwick* [2010] IRLR 244 analysed below.
7 See Frazer 'The employee's contractual duty of fidelity' [2015] LQR 13 (Jan) 53–77.
8 [1895] 2 QB 315.

the judgment, holding that a contract of service contained an implied term that a servant '… will act with good faith towards his master'.

4.9 However, it should be noted that the Court of Appeal founded its conclusion on the earlier decision of the Court of Appeal in *Lamb v Evans*.[9] This latter was a case which concerned whether ex-employees could be restrained from assisting a trade rival by using materials obtained by them whilst employed by the plaintiff. In *Lamb v Evans*, the case was put upon principles of agency, and the relief sought was an injunction after the end of the employment to restrain such use. The issue, held Bowen LJ:

> '… depends entirely … upon the terms upon which the employment was constituted through which the fiduciary relation of principal and agent came into existence … I fully believe that there is no distinction between law and equity as regards the law of principal and agent. The common law, it is true, treats the matter from the point of view of an implied contract, and assumes that there is a promise to do that which is part of the bargain, or which can fairly be implied as part of the good faith which is necessary to make the bargain effectual.'

4.10 Hence, it can be seen that Bowen LJ in *Lamb v Evans* proceeded on the footing that there was no difference between the position in contract and in equity, and that it was appropriate to consider the issue as one of principal and agent. In the same case, Lindley LJ asked, rhetorically, what right an agent had to use materials obtained in the course of his employment against the interest of his employer. He said 'I am not aware that he has any such right. Such a use is contrary to the relation which exists between principal and agent'. Both Lords Justice perceived the matter as falling within the ambit of rules relating to agency and that there was no distinction to be drawn between agents and servants. This absence of differentiation is reflected in a number of early cases but, as Elias J's dictum in *Fishel* shows, is now seen as significant.

4.11 Bowen LJ's dictum was cited with approval by Lord Esher MR in *Robb v Green*. The judgment of Kay LJ in *Robb v Green* makes the same point but by reference to the judgment of Turner VC in *Morrison v Moat*.[10] In *Morrison v Moat*, the plaintiff was granted an injunction to restrain the use of a secret formula, knowledge of which had been shared with a third party under the terms of a contract. The defendant was the recipient of the information from the contract-breaker. The issue was whether 'the court ought to interpose by injunction, upon the ground of breach of faith or of contract'. The Vice Chancellor observed 'That the Court has exercised jurisdiction in cases of this nature does not, I think, admit of any question. Different grounds have indeed been assigned for the exercise of that jurisdiction. In some cases, it has been referred to as property, in others to contract, and in others, again, as founded upon trust and confidence'. He continued 'It was clearly a breach of faith and of contract … to communicate the secret'. Once again, the authority

9 [1893] 1 Ch 218.
10 9 Hare 241.

which underlay the reasoning of Kay LJ was that of twin and undifferentiated duties existing at common law and in equity.

4.12 It may be noted that the authorities which preceded *Robb v Green* had as their subject matter the exploitation of information acquired for limited purposes within the context of a specific relationship. Both law and equity were held by the courts to have the capacity to respond, with the equity's 'breach of faith' being an appeal to fiduciary accountability.[11] However, whatever the source of the obligation, modern statements of the law have clarified that, in an employment context, the implied duty of fidelity is not merely a common law counterpart of a fiduciary obligation. The analysis advanced by Elias J in *Nottingham University v Fishel* commands the field and has been regularly applied and endorsed by the Court of Appeal. In this regard *Customers Systems plc v Ranson* serves to emphasise the distinct treatment required of the contractual and equitable duties.

4.13 That said, it may be noted that in *Kynixa Ltd v Hynes*[12] the duty of fidelity was held to have required of an employee an obligation to report overtures made by a third party to a group senior employees. This is something of a 'high-watermark' case. The other employees within the group owed fiduciary duties. The conclusion that this failure to report was a breach of a contractual term was matched by the judge's conclusion that the other employees who received overtures were in breach of fiduciary duty in failing to report. The demands of loyalty made by fiduciary duties on the one hand and by the implied duty of fidelity on the other thus resulted in a single outcome, consistent, in this respect it may be thought with the approach adopted for example by Bowen LJ in *Lamb v Evans*. However, while the content of the implied duty of fidelity will inform whether there is a fiduciary relationship between employee and employer it remains perilous to infer obligations which are typically imposed on directors – for example duties to report one's own wrongdoing pursuant to s 172 Companies Act 2006 – from the existence of a mere duty of fidelity. In *Item Software v Fassihi*, the Court of Appeal declined to find that a statutory director owed a free-standing reporting duty, preferring instead to base its concusions on the director's duty to act in the best interests of the company, a duty absent from a typical contract of employment. Moreover, in *Ranson v Customer Systems plc*,[13] the Court of Appeal concluded that, whilst it was wrong to say that an employee could never have an obligation to disclose his own wrongdoing, '… any such obligation must arise out of the terms of his contract of employment'.[14] By way of example, the court of Appeal pointed to the express contractual terms which had generated the reporting

11 See contrasting analyses of the juridical basis and treatment of, respectively, the implied duty of fidelity and fiduciary duties in the employment context in Flannigan 'The [Fiduciary] Duty of Fidelity' [2008] 124 LQR 274 and Frazer: The employee's contractual duty of fidelity [2015] LQR 13 (Jan) 53–77.

12 [2008] EWHC 1495 (QB).

13 [2012] IRLR 769.

14 See para 55.

duty in the cases of *Swain v West (Butchers) Ltd*[15] and *QBE Management Services (UK) Ltd v Dymoke*.[16] We analyse in Chapter 2 the extent to which the current law appears to impose positive fiduciary duties of disclosure on directors and certain employees and whether the positive fiduciary duties are consistent with principle or authority.

4.14 A final observation may be made in this context. Since the imposition of fiduciary duties on an employee will depend on the contract and the tasks given to him as a result of that contract, and since the contract is a matter for the parties to agree upon, it follows that the parties can affect the probability that any given employment relationship is accompanied by fiduciary duties. Most employers use standard forms of employment contract and offer employment on a 'take it or leave it' basis. Only in a minority of cases is there any genuine negotiation between the employer and the employee. The bargaining power of a prospective employee is usually quite limited and, consequently, in many cases an employer can, to some degree, legislate for the imposition of fiduciary duties.[17]

The content and limits of the duty of fidelity

4.15 What is the content of the duty of fidelity? If the duty of fidelity requires something less than single-minded loyalty, what are the limits of the demands of loyalty? What is the duration of the duty of fidelity? Are there remedies available only if the employee owes fiduciary duties?

4.16 The short and not very helpful answer to the first of these questions is that the scope of the duty of fidelity can vary from case to case. There is little reliable guidance to be found in the authorities as to what will amount to a breach of the duty of fidelity and as, Lord Greene MR observed in *Hivac v Park Royal*:[18]

> 'The practical difficulty in any given case is to find exactly how far that rather vague duty extends.'

4.17 The ambit of the duty of fidelity will depend upon the contract and the nature of the work required of the employee. The significance of the terms of the contract of employment was emphasised by the Court of Appeal in *Customer Systems*, in which Lewison LJ held that '… both the content of the contractual duty of fidelity and also the existence of any fiduciary duty are determined, in the first instance, by the terms of the employee's contract of employment'.[19] For example, the presence or absence of a 'whole time' clause, requiring the employee to devote the whole of his time and attention to the employer's business, points to a more or a less demanding duty of fidelity. In the

15 [1936] 3 All ER 261.

16 [2012] IRLR 458.

17 See further Chapter 3.

18 [1946] Ch 169.

19 [2012] IRLR 769 at para 35.

CHAPTER 5

UNLAWFUL COMPETITION

INTRODUCTION

Scope of chapter

5.1 Competitive activity by someone owing fiduciary duties exposes a conflict between the interests of the competing entities. In this chapter we consider three often inter-related aspects of competition by a director or employee who owes fiduciary duties which may attract fiduciary liability:

(1) exploitation of corporate opportunities;
(2) preparations for future competition; and
(3) misuse of confidential information.

5.2 Before embarking on a detailed analysis of these three topics we set out a brief overview of the main themes underlying each of these areas.

Corporate opportunities

5.3 'Corporate (or business) opportunity' has no 'term of art' meaning in this context. The factual circumstances in which liability is encountered in this area vary widely: they include at one end of the spectrum the deliberate and dishonest sabotage of commercial negotiations by a director with a view to procuring a distribution contract for himself[1] and at the other the honest and innocent purchase by directors of a company of shares in its newly incorporated subsidiary for the purposes of a transaction benefiting the parent where the parent did not have the means to do so itself.[2] The cases on 'corporate opportunities' reveal four different scenarios which we analyse below:[3]

(1) diversion of the company's/employer's contract or opportunity;
(2) exploitation of an opportunity which comes to the attention of the fiduciary in his fiduciary capacity but which the company/employer cannot exploit;

1
2 *Item Software(UK) Ltd v Fassihi* [2005] 2 BCLC 91; see also *Cook v Deeks* [1916] 1 AC 554.
3 *Regal (Hastings) Ltd v Gulliver* [1967] 2 AC 134.
At 5.47 and following below.

(3) exploitation of an opportunity which comes to the attention of the fiduciary in his private capacity;

(4) post-termination exploitation of a 'maturing business opportunity'.

5.4 Under s 175(1) and (2) of the Companies Act 2006 a director is precluded from exploiting property, information or opportunity where to do so would place him in a situation of potential or actual conflict between his interests and those of the company. 'Information' in this context does not need to derive from the company or even necessarily to be confidential to trigger operation of the provision. This provision is concerned with ensuring that information and opportunities of which a director learns (whether or not by virtue and in the course of his directorship) are not exploited for personal benefit where there is an undisclosed conflict of interest.[4] We consider the issues under the heading 'corporate opportunities'.

5.5 In the United States, a 'corporate opportunity' doctrine has developed. In some states the court will adopt a pragmatic, fact-sensitive and multi-factorial approach towards liability. The good faith of the fiduciary is examined. Absence of good faith is important in establishing liability.[5] Although reference is increasingly made in case law to 'corporate opportunity' cases, English law has developed no analogous 'corporate opportunity' doctrine.

5.6 It is commonly alleged that a director or employee owes a (fiduciary) duty 'not to divert corporate opportunities'. However, no such separate fiduciary duty or head of liability exists. Insofar as case law in this area reveals principled analysis, liability under English law has traditionally been imposed by reference to the 'no conflict' and 'no profit' duties analysed in Chapter 2 and summarised below.[6] These duties operate strictly and the good faith of the fiduciary is irrelevant. The harshness of their operation has been the subject of judicial and academic comment.[7]

5.7 So far as the liability of directors is concerned, it is principally s 175 and not s 176 of the Companies Act 2006 which is relevant to liability for exploitation of corporate opportunities. Section 175 may be understood as having codified both of the equitable 'no conflict' and 'no profit' rules in this context.[8] The codification of the law has not to date caused controversy, and it

4 See *Crown Dilmun v Sutton* [2004] 1 BCLC 468 at para 187.

5 J Lowry and R Edmunds 'The Corporate Opportunity Doctrine: The Shifting Boundaries of the Duty and its Remedies' (1998) 61 MLR 515; see for a consideration of the position in US Law Dr Hans Hirt 'The Law on Corporate Opportunities in the Court of Appeal: *Re Bhullar Bros Ltd*' [2005] JBL 669 at 670 and 683–685.

6 At 5.21–5.24 below.

7 Eg *Murad v Al-Saraj* [2005] EWCA Civ 959; J Lowry and R Edmunds: 'The No-Conflict, No-Profit Rules and the Corporate Fiduciary: Challenging the Orthodoxy of Absolutism' [2000] JBL 122; M Arden 'Reforming the Companies Acts – the Way Ahead' [2002] JBL 579. This harshness has arguably been mitigated by the wording of the 'no profit' duty in s 176(4) of the Companies Act 2006 which does not impose liability where profits have been made unless there was a realistic possibility of a conflict of interest arising.

8 See eg Mortimore *Company Directors: Duties, Liabilities and Remedies* (2nd edn) at

has generally been assumed that there has been no substantive change in the law in this area.[9] We continue to refer to both equitable rules, because it is likely that they will continue to be relevant to the position of employees.

5.8 Prior to the 2006 Companies Act, liability in respect of post-termination exploitation of opportunities had begun to develop by reference to corporate opportunities as 'property' of the company/employer. While such opportunities are not property in the true sense, the law as codified under s 175(2) (and s 170(2)) precludes exploitation of property, information and opportunities of the company even after termination. Information and opportunities are treated analogously to property in this regard.

Preparing to compete

5.9 It is now established that the mere fact that activities carried out by a fiduciary are only preparatory to future competition does not necessarily mean that they will not amount to a breach of fiduciary duty.[10] However, which acts fall the right side of the notional 'liability' line and which the wrong side is not clear. Making a decision to set up a competing business at some point in future and discussing the idea with family and friends will not be a breach of duty; whereas soliciting clients of the company or employer or trading in competition will be a breach of duty. Whether activity between those two ends of the spectrum will engage liability will depend on the facts of the case.[11]

5.10 A director's or employee's preparations to compete create an opposition between the rules of public policy as to restraint of trade on the one hand and equity's strict regulation of fiduciaries on the other. The law strives for a proportionate response, balancing the interests of the individual in free competition with the interests of the company or employer in protecting its business. The law in this area reveals one or other party to have held the balance of power at different times.

5.11 Until relatively recently the law provided a generous ambit within which the employee (and even the director) could operate to prepare for future competition prior to the termination of the fiduciary relationship with his employer or company. Liability was analysed primarily by reference to the 'no conflict' duty. A future interest in a competing company was considered not to amount to a 'conflicting personal interest' for the purposes of that duty.[12] Nor

15.01–15.08; *Palmer on Company Law* at 8-29 (in particular 8.2904). Cf Explanatory Notes to the Act which indicate (at note 338) that the duty replaced (only) the 'no conflict' rule applying to directors.

9 This was the agreed position in *Thermascan Ltd v Norman* [2011] BCC 535; cf *Killen v Horseworld Ltd* [2012] EWHC 363 (QB).

10 *HISL v Tunnard* [2007] IRLR 126.

11 *Shepherds Investments Ltd v Walters* [2007] IRLR 110 at para 108.

12 *Balston Ltd v Headline Filters Ltd* [1990] FSR 385.

was there any prohibition on employees (without more) acting in concert taking steps in preparation for future competition.[13]

5.12 With the development of the law concerning obligations of disclosure[14] the balance of power has swung in recent years, in particular so far as concerns the ability of teams of directors or employees to move lawfully. In *Searle v Celltech*[15] Cumming Bruce LJ had stated (obiter) that:

> 'In the absence of restrictive covenants, there is nothing in the general law to prevent a number of employees in concert deciding to leave their employment and set themselves up in competition with him.'

That approach has been distinguished and largely disapproved. The threat to a business of a proposed team move will mean that, typically, directors and senior employees will be under statutory or contractual obligations to disclose that threat.

5.13 The law concerning directors' and employees' obligations of disclosure has seen considerable development and tightening.[16] However, context is important, and a bifurcation is developing as regards the source of such obligations: in the case of directors it is s 172 CA 2006; the law as regards employees' obligations in this regard cannot be considered settled. Our view is that, even where employees owe fiduciary obligations, disclosure obligations will arise under contract, not in equity.[17]

5.14 In *Foster Bryant Surveying Limited v Bryant & another*[18] Rix LJ adopted a pragmatic approach, acknowledging that where directors retire from office,[19] the circumstances in which they do so are so various that the courts have adopted pragmatic solutions based on a common-sense and merits based approach.[20] He noted that, at one extreme, the director is director in name only.[21] At the other, the director has planned his resignation having in mind the destruction of his company or exploitation of its property.[22] In the middle are

13 *Searle v Celltech* [1982] FSR 92.
14 See as regards directors, albeit not a free-standing duty, but as an incident of s 172 of the Companies Act 2006: *Item Software (UK) Ltd v Fassihi* [2005] ICR 91. See generally *British Midland Tool Ltd v Midland International Tooling Ltd* [2003] 2 BCLC 523; *Shepherds Investments Ltd v Walters* [2007] IRLR 110; *Kynixa v Hines* [2008] EWHC 1495 (QB); *QBE Management Services Ltd v Dymoke* [2012] EWHC 80 (QB), [2012] IRLR 458.
15 [1982] FSR 92.
16 For example, *QBE Management Services Ltd v Dymoke* [2012] EWHC (QB) at para 192.
17 Following *Customer Systems plc v Ranson* [2012] IRLR 769.
18 [2007] EWCA Civ 200, [2007] 2 BCLC 239, [2007] IRLR 425.
19 And, we would add, where an employee's contract of employment terminates.
20 At para 76.
21 *In Plus Group Ltd v Pyke* [2002] 2 BCLC 201.
22 *IDC v Cooley* [1972] 2 All ER 162, [1972] 1 WLR 443; *Canadian Aero Services Ltd v O'Malley* (1973) 40 DLR (3d) 371; *CMS Dolphin Ltd v Simonet* [2001] 2 BCLC 704; *British Midland Tool Ltd v Midland International Tooling Ltd* [2003] 2 BCLC 523.

more nuanced cases which go both ways.[23] A similar fact-specific enquiry applies in the case of employees's preparatory activities in the context of the implied duty of fidelity.[24]

Confidential information

5.15 Directors and employees will frequently be in receipt of information imparted in confidence by the other, because their work will often involve them being made privy to their employer's trade or business secrets. It has been observed that although the existence of the employment relationship explains why the employee comes to be in possession of such information and the employment contract may define the purposes for which such information may be used, the employment relationship itself in such cases is only incidental to the imposition of obligations of confidence.[25] The obligation of confidence often arises in the course of another fiduciary relationship but it is not derived from it. It is for this reason that the obligation of confidence can continue to subsist even when the fiduciary relationship has terminated.[26]

5.16 However, although obligations of confidentiality subsist in equity, those obligations have become at least partly subsumed within a contractual framework. Indeed, the implied duty of fidelity had its origins in the judicial recognition of an obligation to respect confidential material of the employer. We explore the genesis of this development in Chapter 4.[27] As a result, the relationship and boundaries between the implied duty of fidelity, obligations of confidentiality in equity and an implied contractual obligation not to misuse confidential information is not always easy to determine.

5.17 The influential judgments of Goulding J[28] and the Court of Appeal[29] in *Faccenda Chicken v Fowler* have generated a three part test applicable to employment situations which is easily stated but hard to apply: (1) trivial information; (2) information which, if disclosed during employment would amount to a breach of the implied duty fidelity;[30] and (3) trade secrets.[31]

23 *Island Export Finance Ltd v Umunna* [1986] BCLC 460, *Balston Ltd v Headline Filters Ltd* [1990] FSR 385 and *Framlington Group plc v Anderson* [1995] 1 BCLC 475.
24 See *Imam-Sadeque v Blue Bay Asset Management (Services) Ltd* [2013] IRLR 344 at paras 126–132.
25 See *University of Nottingham v Fishel* [2000] ICR 1462 at 1489 per Elias J referring to such obligations of confidence as fiduciary duties. We have avoided this terminology so as to avoid confusion between these obligations and the fiduciary duties which arise under the separate relationship of trust and confidence: see generally Sir Peter Millett 'Equity's Place in the Law of Commerce' (1998) 114 LQR 214 where the three 'fiduciary' relationships are considered: influence, confidentiality and trust and confidence. This work is concerned with the fiduciary duties arising from the relationship of trust and confidence.
26 *Attorney-General v Blake* [1998] Ch 439.
27 See Chapter 4, at 4.7 and following.
28 [1984] ICR 589.
29 [1987] Ch 117.
30 Sometimes described by the conceptually impenetrable epithet 'mere' confidential information. See also *AT Poeton (Gloucester Plating) Ltd v Horton* [2000] ICR 1208.

Following the termination of a fiduciary relationship only trade secrets or information of a comparable degree of confidentiality are protected by the equitable duty of confidence.

5.18 Sometimes, this equitable obligation alone will suffice to preclude a retiring employee or director from exploiting a corporate opportunity. However, the threshold for establishing confidentiality is high, and attempts to dress up what is in reality the skill and knowledge of a director as confidential information have regularly failed.[32]

5.19 We develop the principles and their application in this chapter with a particular emphasis on the impact of obligations of confidence arising in the course of the fiduciary relationship of trust and confidence (loyalty) which is the focus of this work.

THE RELEVANT DUTIES AND THEIR DURATION

5.20 In Chapter 2 we explore the nature and content of fiduciary duties. We summarise the core principles below.

Duties

5.21 It will be apparent from the overview provided above that there are three principal duties[33] which govern the operation of the law in this area:

(1) the 'no conflict' duty;
(2) the 'no profit' duty;
(3) the duty of good faith.

5.22 We consider the equitable obligation of confidence separately below.[34]

No conflict/no profit

5.23 The 'no conflict' and 'no profit' duties are negative in formulation. They are proscriptive. They tell the fiduciary what he is not permitted to do.[35] They do not tell the fiduciary what he is required to do.

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32 *Ixora Trading Inc v Jones & another* [1990] FSR 251 per Mummery J.

33 We consider the implied duty of fidelity below. This is not, of course, a fiduciary duty.

34 At 5.206–5.257 below. This duty is also referred to on occasion as a 'fiduciary duty' – see eg Etherton LJ in *Generics UK Ltd v Yeda Research and Development Co Ltd* [2012] EWCA Civ 726, [2013] Bus LR 777, [2012] CP Rep 39, [2013] FSR 13. Care must be taken to distinguish fiduciary duties of loyalty from fiduciary duties of confidence.

35 *Attorney-General v Blake* [1998] Ch 439.

5.24 These two negative duties can be summarised as follows:

(1) The duty to avoid a situation in which an individual has, or can have, a direct or indirect interest that conflicts, or possibly may conflict, with the interests of his employer (the 'no conflict' duty).[36]

(2) The duty on an individual not, without authority, to make a profit directly or indirectly from the use of property subject to the fiduciary relationship, or in the course of the fiduciary relationship and by reason of his fiduciary position.[37]

5.25 The two duties overlap, but, historically, the better view was that they were to be considered separately.[38] The Companies Act 2006 has codified these duties, as they apply to directors, in ss 175 and 176. However, it would be wrong to view s 175 as the embodiment of the no conflict rule and s 176 as the embodiment of the no profit rule. Section 175 – in particular in its application to the exploitation or property, information and opportunities – embraces the no profit rule.[39] Section 176 is principally applicable to bribes and secret commissions. Although the statutory duties will not apply directly to employees, they have been held to reflect the general law,[40] and not to have effected any material change in the law,[41] and it is not likely that employees will be held to a more stringent code of behaviour than directors.

5.26 Both ss 175(4) and 176(4) of the Companies Act 2006 provide that there will be no breach of duty if, respectively, the situation/acceptance of the benefit cannot reasonably be regarded as likely to give rise to a conflict of interest. This is a refinement to the law, clarifying that the rationale for the duty not to accept benefits is the risk of a conflict between duty and interest. As Sir Peter Millett has put it:[42] 'the second rule (ie the no profit rule) invites the question, "why not?"; the first (ie the no conflict rule) supplies the answer.'

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36 The statutory definition under s 175 Companies Act 2006 includes conflicts between duty and interest and conflicting duties (s 175(7)). Although framed in terms of conflict between interest and interest, the duty has historically been recognised as applying solely to conflicts between duty and interest and duty and duty – see Chapter 2.

37 See para 40 of *O'Donnell v Shanahan* [2009] EWCA Civ 751, [2009] BCC 822 per Rimer LJ. *Chan v Zacharia* (1984) 154 CLR 178 per Deane J at pp 198–199 approved in *Don King Productions v Warren* [2000] Ch 291 at 341 per Morritt LJ and *Ultraframe v Fielding* [2005] EWHC 1638 (Ch) at paras 1305–1306 and 1318.

38 Section 175 was described as having this effect in *Odyssey Entertainment Ltd (in liquidation) v Kamp* [2012] EWHC 2316 (Ch) at para 207.

39 In *Towers v Premier Waste Management Ltd* [2011] EWCA Civ 923, [2012] BCC 72, [2012] 1 BCLC 67, [2012] IRLR 73 Mummery LJ stated, at para 3, that the statutory duties 'extract and express the essence of the rules and principles which they have replaced'. Generally – see Chapter 2.

40 *Thermascan Ltd v Norman* [2009] EWHC 3694 (Ch), [2011] BCC 535, albeit by agreement.

41 'Bribes and Secret Commissions' [1993] RLR 7 at p 9.

Good faith

5.27 The third duty under consideration is the duty to act in good faith in the best interests of the company. This has been held to impose obligations of disclosure on directors[43] and employees[44] to disclose personal wrongdoing and information of interest to the company/employer.

5.28 The nature and extent of this duty and what it requires of a fiduciary remain controversial. While the law regarding directors can be regarded as settled, the extent to which employees may be subject to fiduciary obligations of disclosure is unclear in the light of the decision of the Court of Appeal in *Customer Systems plc v Ranson*.[45] We suggest that the better view is that such duties lie in contract, not equity, and that first instance authority preceding *Ranson* needs to be viewed with care in this respect. The issue is discussed at greater length in Chapter 2.

Duration of fiduciary duties

5.29 The wrongdoing considered in this chapter places a spotlight on activities of the fiduciary which take place shortly before, at the time of, and subsequent to termination of the fiduciary relationship. This requires consideration of the duration of fiduciary duties.[46]

The general rule

5.30 Under the general law, fiduciary duties end with the termination of the relationship which gives rise to them. In *Attorney-General v Blake*[47] the Court of Appeal held as follows:

> 'We do not recognise the concept of a fiduciary obligation which continues notwithstanding the determination of the particular relationship which gives rise to it. Equity does not demand a duty of undivided loyalty from a former employee to his former employer.
>
> ...
>
> These duties last only as long as the relationship which gives rise to them lasts. A former employee owes no duty of loyalty to his former employer. It is trite law that an employer who wishes to prevent his employee from damaging his legitimate commercial interests after he has left his employment must obtain contractual

43 *Item Software (UK) Ltd v Fassihi* [2005] 2 BCLC 91, as an incident of the obligation to act in good faith in the best interests of the company; see now s 172 of the Companies Act 2006.

44 *Hanco ATM Systems Ltd v Cashbox ATM Systems Ltd* [2007] EWHC 1599 (Ch), [2007] All ER (D) 139 (Jul) at para 65 following *Item Software (UK) Ltd v Fassihi*; *Tesco Stores Limited v Pook* [2004] IRLR 618. See also *Governor of Bank of England v Jaffery* [2012] EWHC 1377 (Ch) at para 301; *QBE Management Services Ltd v Dymoke* [2012] EWHC 80 (QB) at paras 186–192.

45 [2012] EWCA Civ 841, [2012] IRLR 769.

46 Considered briefly at Chapter 2, 2.95–2.99.

47 [1998] Ch 439 at pp 453–454.

> undertakings from his employee to this effect. He cannot achieve his object by invoking the fiduciary relationship which formerly subsisted between them. Absent a valid and enforceable contractual restraint, a former employee is free to set up in a competing business in close proximity to his former employer and deal with his former clients. Such conduct involves no breach of fiduciary duty.'

5.31 This approach was echoed by Lord Millett the House of Lords in *Prince Jefri Bolkiah v KPMG*[48] in the context of solicitors' fiduciary duties:[49]

> 'The general rule is that the fiduciary duties terminate with the relationship. The court's jurisdiction cannot be based on any conflict of interest, real or perceived, for there is none. The fiduciary relationship which subsists between solicitor and client comes to an end with the termination of the retainer. Thereafter the solicitor has no obligation to defend and advance the interests of his former client.'

5.32 In both *Blake* and *Bolkiah* it was held that the only duty which survives the termination of the client relationship is a continuing duty to preserve the confidentiality of information imparted during its subsistence.[50]

Liability to account for profits

5.33 Even though the fiduciary relationship has terminated, a fiduciary will still be required to account for unauthorised profits which he earned during the currency of the relationship but which he has not accounted for at the date of termination. He will further be required to account for unauthorised profits which he has earned after the termination of the relationship but which derive from breaches of fiduciary duty occurring before the relationship ended.[51]

5.34 In *Lindsley v Woodfull*[52] (a partnership case) the Court of Appeal explained the basis of a fiduciary's liability to account for profits following termination of the fiduciary relationship. The defendant partner had, in breach of fiduciary duty, diverted a contract from the partnership to his new company, and had not accounted for the profits. It was held to be no answer that he had ceased to be a partner, because the liability to account stemmed from a breach of fiduciary duty while he was still a partner. The profits were consequent thereon.[53] Arden LJ held that, in general, the liability to account extended to the profits earned from renewals by customers or contracts or opportunities wrongfully diverted by the fiduciary, unless there was evidence that the renewals were by reason of something other than the actions of the fiduciary.[54]

48 [1999] 2 AC 222 at p 235.

49 At p 235; cf *Longstaff v Birtles* [2002] 1 WLR 470 which, in espousing the continuation of a fiduciary relationship post-termination of the retainer sits uneasily with this approach.

50 *Blake* at p 454; *Bolkiah* at p 235.

51 *News International plc v Clinger* (unreported) 17 November 1998, ChD per Lindsay J in which the defendant's contentions to the contrary in reliance on the dicta in *A-G v Blake* were rejected – paras 210–212.

52 [2004] EWCA Civ 165, [2004] 2 BCLC 131.

53 At para 28. In fact there was no finding of liability in that case, because of a contractual compromise.

54 See also *Kingsley IT Consulting Ltd v McIntosh & others* [2006] EWHC 1288 (Ch) at para 59.