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EMPLOYEES' AND DIRECTORS' DUTIES

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EMPLOYEES' AND DIRECTORS' DUTIES

THE CONTRACTUAL DUTIES

1. Contracts of employment contain characteristic implied terms. These terms are, as is seen below, essentially of a fiduciary nature. The first two are of long standing, dating back at least to *Robb v Green* [1895] 2 QB 1:

    1.1. the obligation of good faith seems to be effectively the same for both director and employee. The test is a subjective one – it is whether the director or employee considered himself to be acting in the best interests of the company. The classic enunciation for a director (and there is probably no lesser duty on an employee) is that of Lord Greene MR in *In re Smith & Fawcett Limited* [1942] Ch 306:

    > "*The principles to be applied in cases where the articles of a company confer a discretion on directors with regard to the acceptance of transfers of shares are, for the present purposes, free from doubt. They must exercise their discretion bona fide in what they consider - not what a court may consider - is in the interests of the company, and not for any collateral purpose.*"

    1.2. The duty of fidelity (or loyalty) is the duty of good faith's sibling. Primarily, it is concerned with the duty of serving one's employer loyally and faithfully and determines the extent to which, for example, competitive activity during employment is lawful. Again the classic enunciation is that of Lord Greene MR in *Hivac v Park Royal* [1946] Ch 174:

    > *"It has been said on many occasions that an employee owes a duty of fidelity to his employer. As a general proposition that is indisputable. The practical difficulty in any given case is to find exactly how far that rather vague duty of fidelity extends. Prima facie it seems to me on*

considering the authorities and the arguments that it must be a question on the facts of each particular case."

1.3. The obligation of trust and confidence is of little relevance in this context. As was stated by Lord Steyn in *Mahmud v BCCI* [1997] ICR 621H –

> "*There was some debate at the hearing about the possible interaction of the implied obligation of confidence and trust with other more specific terms implied by law. It is true that the implied term adds little to the employee's implied obligations to serve his employer loyally and not to act contrary to his employer's interests.*"

EQUITABLE OBLIGATIONS

2. The traditional view was that it is not the common law but equity that demands and protects good faith and fidelity. Obligations to act in good faith and with fidelity to others are therefore only imposed in narrow circumstances: where fiduciary obligations are imposed.

3. The classic statement is that a fiduciary is expected "to act in the interests of the other—to act selflessly and with undivided loyalty" (Finn, *Fiduciaries Obligations* (1998) p.4.). The obligation to act selflessly is what distinguishes a fiduciary from a person who merely owes contractual obligations. Contractual obligations are not imposed to ensure that people act to the benefit of others. Contractual obligations provide security for the pursuit of self-interest because they are imposed as a result of the objectively viewed intention of the parties rather than those appropriate to someone caring for the property of another.

4. This is reflected in the remedies traditionally awarded. Whereas equity will protect the best interests of the beneficiary of a fiduciary obligation, the common law will only award the victim of a breach of contract what he or she expected to gain from the arrangement.

5. The line between contract and fiduciary duty in employment law is easily blurred and has become significantly more blurred over the last few decades, particularly because employees owe duties of loyalty and good faith. *Harvey* states: "insofar as a servant acts as agent of his employer, the relationship of master and servant is akin to the fiduciary relationship of principal and agent" (A [597]).

6. Even so, the courts have sought to maintain the distinction between contract and fiduciaries in the employment context: *Nottingham University v. Fishel* [2000] IRLR 471 provides an excellent case study.

7. Despite Elias J.'s valiant attempts the distinction cannot be rigidly maintained and the wider quasi-fiduciary obligations are creeping deeper into employment law far beyond company/director relationships.

8. There is **downward pressure**. Fiduciary obligations have crept into ordinary employment relationships.

9. Furthermore, there is also **outward pressure**:

   9.1. the fiduciary obligations of directors have been expanded seemingly beyond the period of service.

   9.2. the development of fiduciary obligations in the employment contract to disclose to an employer one's own breaches of fiduciary duty.

10. There is also **upward pressure**. The law of contract is expanding recovery for gains made by breaching a contract and these have clear implications in the employment sphere.

DOWNWARD PRESSURE – THE FIDUCIARY OBLIGATIONS OF EMPLOYEES

Nottingham University v. Fishel [2000] IRLR 471

11. Dr Fishel was a clinical embryologist and director of a self-funded infertility unit (called Nurture) at Nottingham University. Under the terms of his employment with Nottingham University he was required to receive consent before undertaking paid outside work. In the event Dr Fishel did a considerable amount of work abroad, using staff from Nurture, and arranging remuneration direct (for himself) with foreign clinics. Consent was not sought, but the University was aware of his activities.

12. The clinic at Nottingham University was a success and Dr Fishel received considerable bonus payments. This success was due in no small part to the initiatives of Dr Fishel and its international reputation. After becoming the University's highest paid employee his salary was negotiated downwards and he eventually resigned. The University brought a claim for an account of profits for the work done abroad and for profiting from the work of those under his control at the clinic. This, it was alleged was inconsistent with the undivided loyalty rule and misuse of his position to exploit opportunities to profit.

13. Elias J:

    13.1. In performing outside work without consent Dr F had breached his employment contract. He was liable for damages. However, the university had suffered no loss as it actually gained from his actions

(at [73]). I.e. its expectations had been met and it did not matter that Dr F had made money off the back of them;

13.2. Employee's duty of loyalty and good faith did not entitle employer to be told of work undertaken by employee for profit even if in breach of contract. "Absent the fiduciary obligation, the employee is not obliged to disclose the fact that he has earned sums from third parties" (at [74]).

14. Restitutionary damages could not be awarded, following CA in *A-G v. Blake* Dr F had not done the very thing he had contracted not to do and so the test was not met.

15. As a matter of principle fiduciary and contractual obligations are distinct in the employment context:

> *"…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. The relationship is a contractual one and the powers imposed on the employee are conferred by the employer himself. The employee's freedom of action is regulated by the contract, the scope of his powers is determined by the terms (express or implied) of the contract, and as a consequence the employer can exercise (or at least he can place himself in a position where he has the opportunity to exercise) considerable control over the employee's decision-making powers."* (at 90)

16. However, fiduciary relationships can arise within a particular contractual relationship where there are specific contractual obligations which the employee has undertaken and which place him in a position where equity imposes rigorous equitable duties in addition to his contractual obligations: *"Where this occurs, the scope of the fiduciary obligations both arises out of, and is circumscribed by, the contractual terms; it is circumscribed because equity cannot alter the terms of the contract validly undertaken"* (at [91])

17. “potentially ambiguous terminology” in employment cases “may trap the unwary” (at [91]) The “implied duty of good faith is being used in circumstances where no fiduciary obligation arises at all … the duty is one where each party must have regard to the interests of the other, but not that either must subjugate his interests to those of the other” (at [95]). Care must be taken not to equate duties of trust and confidence or loyalty with fiduciary duties (at [96]).

> *“[I]t is necessary to identify with care the particular duties undertaken by the employee, and to ask whether in all the circumstances he has placed himself in a position where he must act solely in the interests of his employer”* (at [97]).

18. As to breach:

    18.1. If Dr F had treated patients at another clinic in breach of the contractual duty not to compete this may well have “been sufficient to trigger” a fiduciary duty (at [107]),

    18.2. But he was under no duty to secure work abroad and if he had done it in his spare time could not be alleged to breach any fiduciary obligation (at [108]),

    18.3. The money that Dr F earned abroad was paid to him despite his university links not because of it and the money he received was not held on trust (at [112])

    18.4. However, in relation to profits made from work done by other employees of Nurture there was a potential conflict between his “specific duty” to the University to direct them to work for the university and to direct them to work for his own benefit (at [115]). Moreover, he did actually abuse his position in this respect (at [116]). Therefore he was liable for profit made for treatment abroad by embryologists working under his supervision.

19. Despite Elias J's attempt to distinguish fiduciary from contractual obligations his conclusion was that Dr F owed fiduciary obligations

19.1. where he directed employees to work for his benefit,

19.2. if he worked for a competitor, or

19.3. if he made profits by exploiting his position or was paid money in his university capacity.

Each of these examples could conventionally be understood as examples of breach of a fiduciary position. In particular both (.2) and (.3), and probably also (.1), do not appear to have any necessary relation to Dr F's senior position and could apply to any employee (in relation to (.1) any manager). It therefore seems that even where an employee is not in a "fiduciary relationship" equity may impose certain specific obligations of good faith and fidelity.

20. Note that in a leading statement of principle Mason J in the High Court of Australia slipped "employee and employer" amidst the five standard categories:

> *"The accepted fiduciary relationships are sometimes referred to as relationships of trust and confidence or confidential relations (cf. Phipps v. Boardman (1967) 2 AC 46, at p 127), viz., trustee and beneficiary, agent and principal, solicitor and client, employee and employer, director and company, and partners. The critical feature of these relationships is that the fiduciary undertakes or agrees to act for or on behalf of or in the interests of another person in the exercise of a power or discretion which will affect the interests of that other person in a legal or practical sense. The relationship between the parties is therefore one which gives the fiduciary a special opportunity to exercise the power or discretion to the detriment of that other person who is accordingly vulnerable to abuse by the fiduciary of his position. The expressions "for", "on behalf of" and "in the interests of" signify that the fiduciary acts in a "representative" character in the*

exercise of his responsibility" (Hospital Products Ltd v. US Surgical Corp (1984) 156 CLR 41, 96-7)

21. Likewise in *Attorney-General v. Blake* ([1998] Ch. 439, at p. 453) the Court of Appeal accepted without question that the relationship of employer-employee is fiduciary.

22. In *Neary v. Dean of Westminster* [1999] IRLR 288, 290: the mutual duty of trust and confidence was described as a "fiduciary relationship".

23. The two most ignored comments are perhaps the most instructive:

    23.1. In *Henderson v Merrett* [1995] 2 AC 145, 206 Lord Browne-Wilkinson said "The phrase 'fiduciary duties' is a dangerous one, giving rise to a mistaken assumption that all fiduciaries owe the same duties in all circumstances. This is not the case."

    23.2. In *Norberg v Wynrib* (1992) 92 DLR (4th) 449, 481, Sopinka J stated "Fiduciary duties should not be superimposed on those common law duties simply to improve the nature or extent of the remedy".

THE DUTY OF DISCLOSURE OF WRONGDOING

24. The Courts have recently been creating a whole new suite of claims for vindictive former employers. The duty to disclose one's own wrongdoing is the principal weapon in such an employer's armoury.

25. *Bell v Lever Bros* [1932] AC 161 has long been thought to have held that neither an employee nor a director was under no duty to disclose his own wrongdoing:

    "The servant owes a duty not to steal, but, having stolen, is there superadded a duty to confess that he has stolen? I am satisfied that to imply such a duty would be a departure from the well established usage of mankind and would be to create obligations entirely outside the normal contemplation of the parties concerned. If

a man agrees to raise his butler's wages, must the butler disclose that two years ago he received a secret commission from the wine merchant; and if the master discovers it, can he, without dismissal or after the servant has left, avoid the agreement for the increase in salary and recover back the extra wages paid? If he gives the cook a month's wages in lieu of notice can he, on discovering that the cook has been pilfering the tea and sugar, claim the return of the month's wages? I think not. He takes the risk; if he wishes to protect himself he can question his servant, and will then be protected by the truth or otherwise of the answers."

26. Recent decisions have served to undermine the reasoning in relation to employees and re-interpret the comments of their Lordships such that the reasoning is of no application in relation to directors.

27. *Sybron Corp. v. Rochem* [1984] Ch. 112. Held: although the employment contract did not usually require disclosure of own misconduct or that of fellow employees, the terms and nature of the employment might be such that there was a contractual duty to disclose the misconduct of other employees—essentially a fiduciary relationship between senior employee and company, that the position of the defendant as European zone controller was such that he was under a duty to disclose the misconduct of his fellow employees notwithstanding that such disclosure would inevitably disclose his own misconduct.

28. *Van Gestel v. Cann [1987] CL 454*. CA Obiter accepted that directors have positive duty to disclose their wrongdoing.

29. *Tesco Stores Ltd v. Pook* [2004] IRLR 618. D was a senior manager, just below board level, at Tesco. He was responsible for approving invoices. He falsely approved invoices from a company owned and controlled by himself for £512,236. Furthermore, he accepted £323,750 from a company that did business with Tesco. The day before he was dismissed he sought to exercise share options, but he was prevented from doing so. Tesco sued for both amounts. D counterclaimed against the refusal to let him exercise his share options.

30. The court held that the money received from other company was bribe. It gave rise to a conflict of interest and secret profit and it was held on trust for Tesco (at [44]-45]).

31. More controversially, it held that there was an implied term that the share option was not exercisable so long as the employee was in serious breach of contract. Fiduciary obligations could arise in certain limited circumstances, i.e. where a breach of contract has a "fiduciary element":

> *"I accept that there is no duty on an employee to disclose breaches of contract, which do not involve a fiduciary element. However, if an employee receives a profit in breach of his duty, he is liable to account. If he receives a bribe he is liable to account for the bribe. It seems to me that this fiduciary obligation to account is different from the authorities in relation to breaches of contract of employment with no fiduciary element. [63] … I am of the opinion that directors have a positive duty to disclose breaches of their fiduciary duty. I am of the opinion also that senior employees (of the kind identified in Sybron) have a similar duty. I do not believe that the finding of such duties is in conflict with the authorities starting with Bell and following. There is nothing in any of those authorities which suggests that fiduciary duty to account should be treated differently to any other fiduciary duty."*

32. Therefore Mr Pook owed a duty to disclose the bribes he had taken and was in breach of it. The judgment seems to disclose a confusion between the two very different types of fiduciary obligation:

32.1. the fiduciary duty that exists prior to the act complained of such as the broad duty not allow self interest and obligation to conflict;

32.2. the remedial fiduciary obligation to account that is imposed in cases of fraud, bribery or corruption.

33. *Item Software (UK) Ltd v. Fassihi and others* [2004] EWCA Civ 1244, [2004] IRLR 928. This is the clearest and most authoritative enunciation yet of the duty to disclose wrongdoing. Arden LJ stated:

> *"For my part, I do not consider that it is correct to infer from the cases to which I have referred that a fiduciary owes a separate and independent duty to disclose his own misconduct to his principal or more generally information of relevance and concern to it. So to hold would lead to a proliferation of duties and arguments about their breadth. I prefer to base my conclusion in this case on the fundamental duty to which a director is subject, that is the duty to act in what he in good faith considers to be the best interests of his company. This duty of loyalty is the "time-honoured" rule: per Goulding J in Mutual Life Insurance Co of New York v Rank Organisation Ltd [1985] BCLC 11, 21. The duty is expressed in these very general terms, but that is one of its strengths: it focuses on principle not on the particular words which judges or the legislature have used in any particular case or context. It is dynamic and capable of application in cases where it has not previously been applied but the principle or rationale of the rule applies."*

34. The Court went on to hold that a fiduciary in general owed a duty to disclose his own wrongdoing. The court drew an apparent distinction between fiduciaries and ordinary employees, constrained as it was by the decision of the House of Lords in *Bell.*

35. The most difficult question raised by Arden LJ's judgment is that the duty of disclosure is not a freestanding duty but merely an aspect of the duty of fidelity. However, the duty of fidelity seems to be a duty that is both fiduciary and contractual. Given that *Bell* would appear to be binding authority on Arden LJ to the effect that the employee's duty of fidelity imposes no such duty of disclosure it becomes ever harder to see the basis for Arden LJ's judgment.

36. As such, one must resort to the conclusion that the fiduciaries and employees both owe duties of fidelity but the test of infidelity differs between employees and fiduciaries. Surely Lord Atkins' butler cannot have thought that it was in

the best interest of his master for him to remain ignorant of the secret commissions from the wine merchant? Perhaps, one must await the clarification of the degrees of infidelity – lustful thoughts, Caesar's wife's infidelity, Clintonian infidelity and Kimberley Quinn infidelity?

37. At present, the most that can be said is that those who can be classified as fiduciaries will probably held to owe fiduciary duties that encompass disclosure of wrongdoing. Mere employees, particularly if lowly, must still be subject to the general position set out in *Bell*.

IDC V COOLEY LIABILITY

38. Two of the classical fiduciary duties are the duty not to allow one's self interest and the interest of the company to conflict and the duty not to make unauthorised personal gain from one's position as a fiduciary.

39. The principal example of this prohibition on personal gain being applied against directors is *Regal (Hastings) v Gulliver* [1967] 2 A.C. 134. In this case, the plaintiff company owned a cinema in Hastings and wished to purchase 2 further local cinemas in the area with the intention of selling the whole enterprise as a package. In order to do this, a subsidiary with a capital of 5000 £1 shares was formed to take a lease of the 2 cinemas. However, the Company on its own could not raise enough cash in order to obtain the required leases.

40. As the company could not afford to put more than £2,000 into the subsidiary, four of the directors and the company solicitor each subscribed for 500 shares, and the fifth director found some outsiders to take up the remaining 500. The combined concern was then sold (by way of a takeover) and each of the purchasers made a significant profit.

41. The purchasers then brought an (unmeritorious) action against all five of the directors and the company solicitor, claiming that the profits received by each

of these individuals had been obtained through a breach of their respective fiduciary duties, and therefore had to be accounted for to the company.

42. The claim against the director who had not subscribed for any shares obviously failed (as he had made no profit). So too did the action against the company solicitor (as he had subscribed for his shares with the consent of the board of directors as then constituted). However, in the House of Lords the actions against the other four directors succeeded. Lord Russell of Killowen - giving the leading judgment - stated that the directors had *"unquestionably acquired their shares by virtue of their fiduciary position"*.

43. It is essential to note that their Lordships found it immaterial that the company could not itself have subscribed for the shares (and that therefore the company had suffered no loss). The judgment was a straight application of the rule prohibiting fiduciaries profiting from their position(s): whether or not the purchasers had suffered a loss, it was clear that fiduciaries had profited. As stated by Lord Upjohn:

> *"The relevant rule for the decision of this case is the fundamental rule of equity that a person in a fiduciary capacity must not make a profit out of his trust, which is part of the wider rule that a trustee must not place himself in a position where his duty and his interest may conflict".*

44. *Regal* therefore, undoubtedly stands as binding authority for the following principles:

    44.1. that a director owes a fiduciary duty to his company, and

    44.2. that a director who obtains an opportunity by virtue of his fiduciary position is liable to account to the company for his profits.

45. However, there was no doubt on the facts of *Regal* that the Directors had been employed by the company throughout the entire period in question: they had clearly been in a fiduciary relationship with the company throughout the

period in question. *Regal* therefore is not authority for the proposition that the fiduciary duties owed by a director to his company can continue even after his resignation.

46. It appeared that the above additional consideration arose in the case *Industrial Development Consultants Ltd v Cooley* [1972] 2 All ER 162. Here the court was faced with the situation where a company director resigned from the company in order to free himself from his contract of employment, so that he could acquire a valuable contract from a third party business for his own benefit.

47. The facts of the case were that during his time as a director of the Claimant company, the Defendant had been involved in unsuccessful negotiations with the Eastern Gas Board for a contract to design and build certain depots. These negotiations had been unsuccessful primarily for the reason that the Eastern Gas Board objected to the use of consultant organisations (such as the Claimant). However the Eastern Gas Board *was* interested in acquiring the expertise of the Defendant himself and therefore tentatively approached him in his personal capacity.

48. A meeting was arranged for Friday 13th June 1969, where the Defendant was informed of the proposal. He then spent the weekend preparing certain documents in preparation of taking on the contract, and finally, on Monday 16th June, the Defendant informed his current employer that he was on the verge of mental break-down. (He did this in order to obtain an immediate release from his contract of employment). Upon being released, the Eastern Gas Board immediately awarded the contract for the construction of the depots to the Defendant, and the Claimant sued for breach of fiduciary duty.

49. In a straight application of *Regal (Hastings)*, Roskill J found that as a director, the Defendant owed a fiduciary duty to the Claimant:

> *"Therefore, I feel impelled to the conclusion that when the Defendant embarked on this course of conduct of getting information on 13th June, using that information and preparing those documents over the weekend of 14th/15th June*

and sending them off on 17th June, he was guilty of putting himself into the position in which his duty to his employers, the plaintiffs, and his own private interests conflicted and conflicted grievously. There being a fiduciary relationship…it seems to me plain that it was his duty once he got this information to pass it to his employers and not to guard it for his own personal purposes and profit. He put himself into the position when his duty and his interests conflicted".

50. As made clear from the above quotation, Roskill's judgment was fundamentally based on the finding that the Defendant had breached the fiduciary duty he owed *whilst still employed by the Claimant.* It was the Defendant's conduct over the period between 13th June and the date of his resignation that amounted to a breach of fiduciary duty. It was during this period that the Defendant allowed himself to be placed in a position in which his fiduciary duty, and his personal interests conflicted. As made clear by *Regal*, such a position is forbidden in equity: resulting in the liability of the director to account for the profits made, regardless of the fact that the Claimant had suffered no loss.

51. *Cooley* therefore dodged the issue regarding the continuing liability of directors after their resignation, as the judgment was based on the breaches of duty that occurred during the period of the Defendant's employment.

52. In *Island Export Finance Ltd v Umunna and another* [1986] BCLC 460, the Defendant was the managing director of the Claimant (a company which pursued business in West Africa). In 1976, the Defendant secured a contract for the Claimant from the Cameroon Postal Authority (CPA) for postal caller boxes. The contract was for a fixed duration, and although the Claimant hoped for further orders, it had no such assurance from CPA that any further orders would be forthcoming. In 1977, the Defendant resigned as managing director (due to his dissatisfaction with the Claimant rather than his desire to appropriate the Claimant's postal call box business) and set up his own company. At this time, the Claimant was not actively seeking repeat orders from CPA. The Defendant subsequently secured a new contract with CPA for

his own company. The Claimant sued for the Defendant's alleged breach of fiduciary duty.

53. The importance of this case arises from the fact that during his judgment Hutchison J, recognised that the law as set out in the Canadian case of *Canadian Aero Service v O'Malley* (1973) 40 DLR (3d) 371, was an accurate description of the present aw in England. In particular, Hutchison J relied on the following excerpt of Laskin J's Judgment in above case:

> *"…a…director is precluded from obtaining for himself, either secretly or without the approval of the company…any property or business advantage either belonging to the company or for which it has been negotiating…In my opinion, this ethic disqualifies a director or senior officer from usurping for himself or diverting to another person or company with whom or with which he is associated a maturing business opportunity which his company is actively pursuing; he is also precluded from so acting even after his resignation where his resignation may fairly be said to have been prompted or influenced by a wish to acquire for himself the opportunity sought by the company,* ***or [and]*** *where it was his position with the company rather than a fresh initiative that led him to the opportunity which he later acquired"*

54. Hutchison J recognised the above to represent the law of England, with the exception that it was his belief that it was likely that Laskin J meant 'and' rather than 'or' in the above passage, in that the use of this word was probably meant as indicating the element of causation necessary to make the resignation to make the director liable, and not indicating a separate ground for making him liable. As Hutchison went on to state:

> *"It would…be surprising to find that directors alone, because of the fiduciary nature of their relationship with the company, were restrained from exploiting after they had ceased to be such, any opportunity of which they had acquired knowledge while directors. Directors, no less, than employees, acquire a general fund of knowledge and expertise in the course of their work, and it is plainly in the public interest that they should be free to exploit it in a new position".*

55. It seems to me therefore, that the effect of *Umunna* is to hold that the ordinary fiduciary duty owed by a director to his company is capable of surviving the director's resignation *in certain circumstances.* These circumstances being:

55.1. Where there exists 'a maturing business opportunity' enjoyed by the company; and

55.2. Where this opportunity is being actively pursued by the company; and

55.3. Where the director's resignation was prompted/influenced by his wish to acquire for himself the opportunity/where it is the directors position with the company rather than a fresh initiative that led him to the opportunity.

56. Hutchison J therefore applied the above principles to the facts of the case, and held that the Claimant's claim failed for three simple reasons. Firstly, the hope of obtaining further orders from CPA could not, in any realistic sense be said to be 'a maturing business opportunity'; secondly at the time of the Defendant's resignation the Claimant was not actively pursuing the matter; and thirdly, Hutchison J found that the reason why the Defendant resigned was due to his dissatisfaction with the Claimant, rather than his desire to steal their business.

57. At first reading there appears to be a clear tension between this decision, and the law as stated in *Regal*. In Regal it was held that *the only* issue was whether the fiduciary had profited from his breach of duty – whereas *Umunna* suggests that a director can defend a claim of breach of fiduciary duty by showing that the company was not actively pursuing the business at the time of his resignation. This appears to be at variance with the *Regal* decision because it is clear from that case that such factors are irrelevant, and regardless of the actions of the company, the fiduciary is forbidden from profiting from his position.

58. In my opinion however, this tension may be illusory. *Umunna* is not authority that in general the fiduciary duties of a director continue regardless of his resignation. As was acknowledged in *Simonet* and in *A-G v Blake (Jonathan Cape Ltd, third Party)* [1998] 1 All ER 833 at 841:

58.1. A director's power to resign from office is not a fiduciary power; and

58.2. In general a fiduciary relationship does not continue after the determination of the relationship which gives rise to it.

59. *Umunna* is authority for the principle that only in the circumstances outlined above in paragraph 55 will a director remain in a fiduciary relationship with his ex-employers notwithstanding his resignation. The issues raised by *Umunna* are therefore considerations in relation to whether or not a fiduciary relationship continues to exist. Once the continuing fiduciary relationship is established (under *Umunna)* then the director's liability to account is confirmed, and questions of causation and whether the company has suffered a loss cease to be relevant. However, it is submitted that these very issues that are irrelevant *after* the establishment of the relationship, may be fundamental to the question of whether or not the fiduciary relationship continues after the director's resignation.

60. In my view, a strong argument can be made to suggest that the cases of *Regal* and *Umunna/O'Malley* deal with different considerations: the former dealing with the effect of a breach of fiduciary duty by a director, and the latter deciding whether or not such a relationship existed between the company and the director, once he had resigned.

61. To a significant extent, *CMS Dolphin Ltd v Simonet* [2001] 2 BCLC 704 supports the above interpretation of the law. In expressly applying the law set out in *O'Malley*, Collins J held that a director is disqualified from usurping for himself or diverting to a company with which he is associated a 'maturing business opportunity' of his company, not only while he is still a director, but also even

after his resignation, where the resignation may fairly be said to have been prompted or influenced by his wish to acquire the opportunity for himself.

62. In fact, Collins J went further, holding that:

> *"In my judgment the underlying basis of the liability of a director who exploits after his resignation a maturing business opportunity of the company is that the opportunity is to be treated as if it were the property of the company in relation to which the director had fiduciary duties. By seeking to exploit the opportunity after resignation he is appropriating for himself that property. He is just as accountable as a trustee who retires without properly accounting for the trust property. In the case of the director he becomes a constructive trustee of the fruits of his abuse of the company's property, which he has acquired in circumstances where he knowingly had a conflict of interest, and exploited it by resigning from the company"*

63. On the one hand therefore, *Simonet* represented a whole-hearted concurrence (with *Umunna*) that *O'Malley* represents the current state of English law regarding the fiduciary duties owed by directors to their companies after resignation.

64. On the other hand, however, it seems that by treating the business opportunity as the 'property' of the company, there is a good chance that Collins J has significantly widened the principle. As the company 'owns' this opportunity, it could well be argued that by reason of the knowledge obtained during his employment, a director who has decided to resign from his company in order to compete for that company's business may well be barred from taking such action for an indeterminate period.

65. Equally, *Simonet* offers little guidance regarding how a court would calculate the amount of profit that a director would need to account to the company where he had breached his fiduciary duty by successfully taking on a 'rolling' contract with one of the company's current customers. In such a situation,

where the life of the contract is capable of continuing into the distant future, the only guidance offered by *Simonet* is that "*there must be some reasonable connection between the breach of the duty and the profits for which the fiduciary was accountable*".

66. Such practical issues aside, in my opinion, *Simonet* confuses the basic issues involved in demarcating the duties owed by directors. At paragraph 87 of his judgment, Collins J describes the basic issue of law involved in the above case in the following terms:

> *"The present case concerns the question of how far the principle in Regal (Hastings) Ltd v Gulliver extends to a director who resigns his office to take advantage of a business opportunity of which he has knowledge as a result of having been a director".*

67. Granted, at a basic level this is a fair description of the issue involved in the case. The problem lies in the fact that he then attempts to show that the principles involved in analysing this question date back to at least to *Cooley*, if not *Regal* itself.

68. It seems to me that there was never any doubt that *if* the director continued to be under a fiduciary duty after his resignation, then the principles set out in *Regal* would be directly applicable. The *only* novel question with which Collins J had to wrestle (in respect to the fiduciary duty question) was *whether* - on the facts of the case - the fiduciary duty survived the director's resignation. The facts put forward by Simonet were that he was bound by no covenants, he resigned and thereafter was free to compete so long as he had not misused confidential information.

69. The answer to *this* question simply could not be found in *Cooley* as Roskill had been extremely careful not to found his judgment on anything outside the acts of the director in question during the period of his employment.

70. It is therefore my opinion that attempting to find the principles in the older cases, Collins J confused the issues regarding the consequences of breaching a

fiduciary duty and the separate issue of whether on not such duties survived the resignation of the director. The answer to this latter question, in my opinion, can only be traced back to either *Umunna*, or *O'Malley* itself.

71. Since 2001, *Simonet* has been considered by the English courts on a number of occasions. Each of these cases has added little to the principles outlined in *Simonet. Hunter Kane Ltd v Watkins* [2003] All ER (D) 144 Feb, however offers a helpful summary of the current state of the law, following Collins J's judgment:

71.1. A director while acting as such, has a fiduciary relationship with his Company. That is he has an obligation to deal towards it with loyalty, good faith and avoidance of the conflict of duty and self-interest.

71.2. A requirement to avoid a conflict of duty and self interest means that a director is precluded from obtaining for himself, either secretly or without the informed approval of the Company, any property or business advantage either belonging to the Company or for which it has been negotiating, especially where the director or officer is a participant in the negotiations.

71.3. A director's power to resign from office is not a fiduciary power. He is entitled to resign even if his resignation might have a disastrous effect on the business or reputation of the Company

71.4. A fiduciary relationship does not continue after the determination of the relationship which gives rise to it. After the relationship is determined the director is in general not under the continuing obligations which are a feature of the fiduciary relationship.

71.5. Acts done by the directors while the contract of employment subsists but which are preparatory to competition after it terminates are not necessarily in themselves a breach of the implied term as to loyalty and fidelity.

71.6. Directors, no less than employees, acquire a general fund of skill, knowledge and expertise in the course of their work, which is plainly in the public interest that they should be free to exploit it in a new position. After ceasing the relationship by resignation or otherwise a director is in general (and subject of course to any terms of the contract of employment) not prohibited from using his general fund of skill and knowledge, the 'stock in trade' of the knowledge he has acquired while a director, even including things such as business contacts and personal connections made as a result of his directorship.

71.7. A director is however precluded from acting in breach of the requirement at 2 above, even after his resignation where the resignation may fairly be said to have been prompted or influenced by a wish to acquire for himself any maturing business opportunities sought by the Company and where it was his position with the Company rather than a fresh initiative that led him to the opportunity which he later acquired.

71.8. In considering whether an act of a director breaches the preceding principle the factors to take into account will include the factor of position or office held, the nature of the corporate opportunity, its ripeness, its specificity and the director's relation to it, the amount of knowledge possessed, the circumstances in which it was obtained and whether it was special or indeed even private, the factor of time in the continuation of the fiduciary duty where the alleged breach occurs after termination of the relationship with the Company and the circumstances under which the relationship was terminated, that is whether by retirement or resignation or discharge.

71.9. The underlying basis of the liability of a director who exploits after his resignation a maturing business opportunity of the Company is that the opportunity is to be treated as if were the property of the Company in relation to which the director had fiduciary duties. By seeking to

exploit the opportunity after resignation he is appropriating for himself that property. He is just as accountable as a trustee who retires without properly accounting for trust property.

71.10. It follows that a director will not be in breach of the principle set out in 7 above where either the Company's hope of obtaining the contract was not 'a maturing business opportunity' and it was not pursuing further orders nor where the director's resignation was not prompted or influenced by a wish to acquire the business for himself.

71.11. As regards breach of confidence, although while the contract of employment subsists a director or other employee may not use confidential information to the detriment of his employer, after it ceases the director/employee may compete and may use know-how acquired in the course of his employment (as distinct from trade secrets – although the distinction is sometimes difficult to apply in practice).

72. In conclusion, due to the impact of *Simonet* and *Umunna*, this area of the law is dogged by uncertainty, and as a result it remains difficult to advise a company director as to his liability where he has resigned, and intends to set up business in competition with his ex-employers.

73. In my understanding of the law, once a director has resigned, the fiduciary duties owed to the company cease, except in the three situations outlined in *Umunna*: the fiduciary duties survive the resignation only where the Director has *decided to resign specifically to steal the company's business.* In my opinion, where the company does not possess any chance of obtaining that business, there seems little reason why the director should be under a fiduciary duty forbidding him from going after it *once he has resigned* but that is, at present, inconsistent with the decision in *Simonet.*

74. This would not be in conflict with the rule in *Regal*, as the question of whether or not the company has any chance of obtaining the business for itself (post

resignation) would be a question in relation to establishing the existence of a fiduciary relationship rather than a defence/a reason why damages should be reduced.

75. Perhaps the simple answer to this issue is that each of the cases that have come before the court have been found to have a 'slight' chance of obtaining the business. Perhaps in a situation where that chance was in fact zero, the courts would find that there was no maturing business opportunity.

SPRINGBOARD RELIEF

76. Others will be dealing with springboard injunctions. These are generally (and traditionally) sought in cases involving misuse of confidential information. It should be noted that there is a wholly unreported but well reasoned decision of Blackburne J to the effect that breaches of fiduciary duty may ground a claim for springboard relief - *Midas IT Services v Opus Portfolio Limited*, 21st December 1999.

RESTITUTIONARY REMEDIES

77. *AG* v. Blake [2001] 1 AC 268:

> "Equity reinforces the duty of fidelity owed by a trustee or fiduciary by requiring him to account for any profits he derives from his office or position. This ensures that trustees and fiduciaries are financially disinterested in carrying out their duties. They may not put themselves in a position where their duty and interest conflict. To this end they must not make any unauthorised profit. If they do, they are accountable. Whether the beneficiaries or persons to whom the fiduciary duty is owed suffered any loss by the impugned transaction is altogether irrelevant. The accountability of the army sergeant in Reading v Attorney General

[1951] AC 507 is a familiar application of this principle to a servant of the Crown." p.280 per Lord Nicholls.

"My conclusion is that there seems to be no reason, in principle, why the court must in all circumstances rule out an account of profits as a remedy for breach of contract. I prefer to avoid the unhappy expression "restitutionary damages". Remedies are the law's response to a wrong (or, more precisely, to a cause of action). When, exceptionally, a just response to a breach of contract so requires, the court should be able to grant the discretionary remedy of requiring a defendant to account to the plaintiff for the benefits he has received from his breach of contract. In the same way as a plaintiff's interest in performance of a contract may render it just and equitable for the court to make an order for specific performance or grant an injunction, so the plaintiff's interest in performance may make it just and equitable that the defendant should retain no benefit from his breach of contract." (284-285 per Lord Nicholls)

78. In so holding the House of Lords blurred the distinction between fiduciaries and mere contractors/employees. Significantly the analogy relied upon to justify the court's ability to award an "account"—which is an equitable remedy—was specific performance—which is, of course, also an equitable remedy.

79. Blake's case was held to be exceptional because he had used confidential information, against repeated instructions, for his own benefit and to great damage to the public interest (supposedly). Lord Steyn stated that he was "in a very similar position to a fiduciary. The reason of the rule applying to fiduciaries applies to him." (p.292).

80. The precise nature of the award of an account and its extent was left to be "hammered out on the anvil of decided cases" (per Lord Steyn p. 291)

81. *Experience Hendrix LLC v. PPX Enterprises Inc* [2003] EWCA Civ 232. As in *Blake*:

81.1. There was a breach of a negative obligation, and PPX had done the very thing it had contracted not to do.

81.2. PPX knew that it was doing something which it had contracted not to do.

81.3. Injunction or specific performance could not provide an effective remedy and the failure to claim one in the past is not the claimant' fault.

82. However, at paragraph 37 Mance LJ outlined some important difference with Blake:

82.1. Not concerned with a subject anything like as special or sensitive as national security.

82.2. The notoriety which accounted for the magnitude of Blake's royalty earning capacity derived from his prior breaches of secrecy, and that too had no present parallel.

82.3. No direct analogy between PPX's position and that of a fiduciary.

83. In addition, great weight was put on the fact that, though deliberate, the breaches were in the "commercial context" in the course of business to make a profit and had to expend some skill and money (at[44]).

84. For these reasons the Court of Appeal ordered only that PPX pay a reasonable sum to Hendrix. Mance LJ:

> *"For the past, in the absence of any proven loss, I would confine any financial remedy to an order that PPX pay a reasonable sum for its use of material in breach of the settlement agreement. That sum can properly be described as being "such sum as might reasonably have been demanded" by Jimi Hendrix's estate "as a quid pro quo for agreeing to permit the two licences into which PPX entered in breach of the settlement agreement", which was the approach adopted*

by Brightman J in Wrotham Park (cf paragraph 22 above). This involves an element of artificiality, if, as in Wrotham Park, no permission would ever have been given on any terms."([45])

85. Peter-Gibson LJ stated:

> *"I do not think the present case an appropriate one for ordering an account of profits. He has drawn attention in para. 37 above to the features of the present case which distinguish it from the circumstances in Blake. No doubt deliberate breaches of contract occur frequently in the commercial world; yet something more is needed to make the circumstances exceptional enough to justify ordering an account of profits, particularly when another remedy is available."([55])*
>
> *"In my judgment, because (1) there has been a deliberate breach by PPX of its contractual obligations for its own reward, (2) the claimant would have difficulty in establishing financial loss therefrom, and (3) the claimant has a legitimate interest in preventing PPX's profit-making activity carried out in breach of PPX's contractual obligations, the present case is a suitable one (as envisaged by Lord Nicholls ([2001] 1 AC at pp. 283H – 284A) in which damages for breach of contract may be measured by the benefits gained by the wrongdoer from the breach. To avoid injustice I would require PPX to make a reasonable payment in respect of the benefit it has gained." ([58])*

86. As such, these two remedies are particularly important in breach of confidence and covenant cases where damage to the claimant may be hard to prove but profIt may have been obtained by the defendant.

FINAL ISSUE-EXEMPLARY DAMAGES FOR BREACH OF FIDUCIARY AND CONTRACTUAL DUTIES

87. *Harris v Digital Pulse Pty Ltd* [2003] NSWCA 10. The respondent conducted an information technology business called Digital that included Web design. The

appellants Harris and Eden were employed in marketing and web design respectively. Commencing in December 1999, they worked secretly for the benefit of their own business, which was incorporated as "Juice" on 27 January 2000. Using their employment as a springboard they did projects for existing or potential clients of Digital. In some cases those clients were charged a fee, being invoiced by Juice. Harris was dismissed on 4 February 2000 and Eden resigned the next day.

88. Palmer J held that there had been breaches of both contractual and fiduciary duties of loyalty and the respondents were entitled to an account or compensation at their election. They elected an account but still only a very low amount was recovered—probably less was uncovered than the amount actually made. Relying on Kuddus, he therefore held that respondents were additionally entitled to an award of punitive damages since the employees had acted with conscious dishonesty, in breach of positions of trust and responsibility, and in a manner calculated to produce harm to their employer and profit to themselves (at [118]-[140]

89. The New South Wales Court of Appeal overturned the award of punitive damages. The majority held that the award could not be justified by pointing to any previous authority. Heydon JA, suggested that exemplary damages should never be available for breach of fiduciary duty (at [470]). However, each of the judgments were careful to limit the holding to the specific circumstances of the case. Spigelman J. noted that "Remedial flexibility is a characteristic of equity jurisprudence" (at [4]).

90. The most interesting (and persuasive) judgment is Mason P.'s dissent. His Lordship held that equity should be prepared to strive for remedial adequacy, that the tort analogy is forceful, and that it should be followed in the interests of conceptual coherence (at [212]-[213]). The further comments are of wider significance and no doubt will have to be considered by English courts and either followed or rejected in due course:

> 134 In this case, although the damage inflicted on the Plaintiff is relatively modest in monetary terms, the character of the Defendants' dishonest conduct strikes at the heart of commercial integrity, upon which the business community, and ultimately the community as a whole, depends. Employers should feel able to entrust their business confidences to their employees with security. Employees should know that deliberate and dishonest breach of their fiduciary duties of loyalty, calculated to produce profit for themselves, will not go unpunished and that, at the end of the day, breach of those duties does not pay. …
>
> 169 In my opinion, the present position in Australia can be summarised thus. There is no authority which decides that exemplary damages cannot, as a matter of principle, be given by a court of equity for breach of fiduciary duty. Accordingly, to hold that wrongful conduct which would attract an award of exemplary damages in an action in tort cannot attract exemplary damages if the cause of action is equitable creates an anomaly which, in this country, is not justifiable either by precedent or by principle.
>
> 170 Consistency in the law requires that the availability of exemplary damages should be coextensive with its rationale. Where wrongful and reprehensible conduct calls for the manifest disapprobation of the community, where a punishment is called for to deter the wrongdoer and others of like mind from similar conduct and where something more than compensation is felt necessary to ameliorate the plaintiff's sense of outrage, then it should make no difference in the availability of exemplary damages that the court to which the plaintiff comes is a court of equity rather than a court of common law.

91. Similarly, the Canadian courts have recently awarded exemplary damages in a contract case – *Royal Bank of Canada v Got* 178 DLR (4th) 385 (2000).

92. Whilst the English courts sought to limit the availability of exemplary damages in tort cases in *Rookes v Barnard* [1964] AC 1129, and pronounced that such damages were not available in the contract field in *Addis v Gramophone* [1909] AC 488, the tide does seem to be turning once more in favour of the award of exemplary damages opening up the prospect of such damages being available in extreme cases for breach of fiduciary duty and possibly even for breaches of contract at some point in the future.

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Thanks are due to Tom Hickman for his research on aspects of this paper. The errors are all mine.