Fiduciary Duties: Directors and Employees

Second Edition

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PREFACE TO THE SECOND EDITION

We wait decades for a House of Lords/Supreme Court decision in the field of fiduciary duties and, like buses, they all come at once. In the immediate aftermath of publication of the first edition of this work, there was little significant development in English fiduciary law relating to directors and employees. However, with the passing of the 'noughties' a wave of important appellate law has swept in. There is no chapter of this book whose subject matter has not been the subject of extended treatment by the Supreme Court or Court of Appeal. This has led to a substantial rewriting of many parts of the text.

Publication of the first edition coincided with the coming into force of the directors' duties under the Companies Act 2006. However, in the interim Australian law has seen more controversy concerning the nature and ambit of directors' duties than English law.

The Western Australia Court of Appeal's monumental decision arising out of the liquidation of the Bell Group (*Bell Group (in liquidation) v Westpac Banking Corp*[1]) has generated a detailed and sustained treatment of the nature and function of directors' duties, holding that in Australian law, directors' fiduciary duties are not limited to negative, proscriptive duties contrary to the case advanced by the defendant banks in reliance on the well-known Australian High Court decision in *Breen v Williams*.[2]

In another notable and already frequently cited Australian decision of Finn J[3] in the Federal Court, *Grimaldi v Chameleon Mining Corp & Others*,[4] a helpful distinction has been drawn between two strands of fiduciary law – the law concerning fiduciary loyalty on the one hand and the law governing exercise of discretionary powers by fiduciaries on the other.

These decisions serve to confirm that, notwithstanding the developments in the law in recent years, it remains critical to determine the context in which, and the purpose for which, one is seeking to determine whether a 'fiduciary' duty exists. Notwithstanding continued widespread support of the decision of

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1 [2012] WASCA 157.
2 Permission to appeal to the High Court was obtained, but the case settled prior to the hearing.
3 Author of the seminal 1977 work on fiduciary duties.
4 [2012] 287 ALR 22.

Millett LJ in *Bristol & West Building Society v Mothew*[5] there remains controversy over the content of fiduciary obligation.

The approach and methodology by which employees are held to owe fiduciary duties has received considerable and broadly consistent illustration at first instance applying the approach in *Nottingham University v Fishel*. The importance of establishing an employee's role, function and tasks in this regard can be seen to be critical.

While the content of fiduciary obligation imposed on employees is not settled, happily, with the Court of Appeal decision in *Ranson v Customer Systems plc,*[6] a line has been drawn in the sand clarifying that merely to hold an employee to be a fiduciary does not automatically subject him or her to the full range of directors' duties.

The Supreme Court in *Revenue and Customs Commissioners v Holland*[7] has reviewed the law on de facto directors in the context of corporate directors, an area which we consider in Chapter 2.

Uncertainties as to the meaning of 'trust' and 'trust property' in s 21 of the Limitation Act have also been resolved by the Supreme Court in *Williams v Central Bank of Nigeria*[8] such that the law of limitation in this field has now been settled.

In *Vestergaard Frandsen v Bestnet*[9] the Supreme Court considered the scope of the equitable duty of confidence and proof of the mental requirement to establish a breach of such duty.

Attribution of knowledge, and, in particular, the 'fraud exception' or '*Hampshire Land*' principle has also been under the lens of both the House of Lords in the difficult decision in *Stone & Rolls Ltd (in Liquidation) v Moore Stephens (A Firm)*[10] and the Court of Appeal (considering its application) in *Bilta (UK) Ltd v Nazir.*[11]

The law of bribery has seen sustained treatment in a number of substantial commercial fraud actions at first instance, and the principles have been extensively reviewed.

However, it is in the areas of remedy that there has been the greatest development in the law since the first edition.

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5 [1998] Ch 1.
6 [2012] EWCA Civ 841.
7 [2010] UKSC 51.
8 [2014] UKSC 10.
9 [2013] UKSC 31.
10 [2009] UKHL 39.
11 [2013] EWCA Civ 968; following a hearing in October 2014, judgment in the Supreme Court is awaited.

The Supreme Court decisions in *VTB Capital plc v Nutritek International Corp*[12] and *Prest v Petrodel Resources Ltd*[13] have particular application in the case of defaulting fiduciaries in clarifying the principles concerning 'piercing the corporate veil'. *Prest* provides a luminous explanation of the 'evasion' and 'concealment' principles. It is a welcome addition to the fraud lawyer's toolkit, stripping away unclarity concerning the meaning or application of concepts such as 'alter ego', 'sham' and 'façade' companies when considering the role or liability of wrongdoers and their associated corporate entities.

The decision in *Grimaldi* contains a comprehensive and pellucid statement of the relevant principles underlying many aspects of modern fiduciary law as applicable to directors and employees. It is particularly instructive in its treatment of the difficult (and much under-explored) area of accounting for 'business' profits where there are mixed sources of profit and difficulties of attribution.

The case of *Sinclair v Versailles* and its treatment of the remedies available in respect of bribes and secret commissions – and in particular two irreconcilable lines of authority: *Lister v Stubbs* (debt) and *Attorney-General v Reid* (constructive trust) – has provoked heated and stimulating controversy and debate in case-law and among practitioners and academics. The Supreme Court in *FHR European Ventures LLP v Cedar Capital Partners LLC*[14] has finally resolved this debate. The decision has the great advantage of being 'right because it is final [as] there is precious little prospect of agreement on a judgment that is final because it is right'.[15] The decision has established that unauthorised profits held by a fiduciary will be held on constructive trust. It is to be welcomed as much for its result as for the manner of its communication – short, unanimous and unequivocal.

The net effect of the above developments mean that even if the expression 'constructive trust' still carries decades of historical baggage there is a now a much clearer body of law explaining what should be understood by the term in different contexts and what rights and limitations apply.

The compensatory regime (albeit in the context of a commercial trust involving solicitors) has also been considered in detail by the Supreme Court in *AIB Group (UK) Plc v Mark Redler & Co Solicitors*.[16] The decision follows and clarifies the decision of the House of Lords in *Target Holdings Ltd v Redferns*. It is likely that this decision will be no less controversial than that in *Target Holdings*, in affirming the potential relevance of causation even in cases where trust property has been misapplied and where restoration of the property or 'restitutive' compensation has traditionally been considered to be the primary remedy.

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12 [2013] UKSC 5.
13 [2013] UKSC 34.
14 [2014] UKSC 45.
15 Nolan 'Bribes: a reprise' (2011) 127 LQR 19, 23.
16 [2014] UKSC 58.

There have been a number of helpful decisions clarifying the practical as well as jurisprudential distinctions between an account and an account of profits, as well as an illustration of the practical effect of what burdens will face directors required to account for their dealings with company property. Recent cases also point up the conceptual and practical distinctions between the (objective) 'no conflict' and 'no profit' duties and the (largely) subjective test to be applied when looking at the discretions fettering a director's decision-making.

Forfeiture of fiduciary remuneration is an area which has had new life breathed into it following *Imageview Management Ltd v Jack*.[17] Fiduciaries remain largely ignorant of the risk that, in respect of disloyal behaviour they may not only be required to account for profits made or to compensate loss sustained, but may additionally forfeit remuneration paid in respect of the transaction or conduct which has given rise to the disloyal conduct.

If the scope of the remedial regime in respect of accessories is still open to debate, the current direction of travel is clearer than it was as a result of the decision of the Court of Appeal in *Novoship (UK) Ltd v Mikhaylyuk*.[18] This case is an off-shoot of the long-running *Fiona Trust* litigation – a gift to the legal profession which keeps on giving. The decision is likely to provoke controversy, not least for: its statement that there are different nexus/causation thresholds applicable to fiduciaries and (a more rigorous threshold) to accessories when assessing damages and an account of profits; its holding that an account of profits will not be available automatically against accessories (mirroring the approach in relation to those who misuse confidential information); the introduction of a remoteness test for the recovery of equitable compensation from accessories (arguably inconsistently with the discussion underpinning the subsequent decision of the Supreme Court in *AIB*). Against a judicial climate which has generally confirmed a continued hardening of attitudes against bribery and corrupt commercial conduct this decision blows a surprisingly warm wind over the treatment of third parties involved in such conduct.

In the first edition we raised the question of the application to directors and employees of the '*Bolkiah*'/'Chinese Walls' principle crystallised in the House of Lords decision in *Prince Jefri Bolkiah v KPMG*.[19] The Court of Appeal roundly rejected application of the *Bolkiah* principle to employees in *Caterpillar Logistics (Services) UK Limited v Huesca de Crean*.[20] It was also (though less roundly) rejected in the case of an employed patent attorney in *Generics (UK) Ltd v Yeda Research and Development Co Ltd*.[21] The principles have not been tested in the context of directors, but it would appear unlikely that such an approach will find favour.

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17 [2009] EWCA Civ 63.
18 [2014] EWCA Civ 908.
19 [1999] 2 AC 222.
20 [2011] EWCA Civ 1671.
21 [2012] EWCA Civ 726.

There have also been important incremental developments in the remedial regime for breach of contract, considered in Chapter 4. The (welcome) trend at first instance has been to adopt an increasingly broad approach to the availability of springboard injunctive relief to cancel out unlawful headstarts (however obtained) and 'restitutionary' or 'hypothetical release' damages following the *Wrotham Park* line of case-law. Such remedies have a particular resonance in cases of unlawful business competition where there have been breaches of duties of loyalty, misuse of confidential information or breach of post-termination restrictive covenants and where loss may be difficult to establish.

Since the first edition there has continued to be a large volume of stimulating and thought-provoking academic commentary published. It is daunting for practitioner authors to keep abreast of developments in thinking. We have sought, where possible, to reflect comment, and we express our debt to the writings which have helped to inform this work, in particular those of Matthew Conaglen, Richard Nolan, Charles Mitchell, Paul Davies, Lionel Smith and James Edelman.

We have endeavoured to state the law as at 31 December 2014.

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