PART II — FIDUCIARY RELATIONSHIPS

I *Introduction*

A *The Meaning of 'Fiduciary'*

The word 'fiduciary' derives from the Latin *fiducia*, meaning 'trust'. In equity, it is used in at least four different senses; namely, to:

1. Describe the position of a person who in equity owes 'fiduciary obligations';
2. Denote the special character of a relationship between a fiduciary (used in the first sense) and their principal (the person to whom they owe obligations);
3. Denote the character of an obligation owed by one person to another as falling within the class of duties which in equity are viewed as 'fiduciary', breach of which will give rise to a remedy for breach of fiduciary duty; and
4. Express that particular circumstances are such as to create a fiduciary (used in the second sense) relationship.

Certain *judicial aberrations* notwithstanding, the essence of a fiduciary relation is true to its name, being *trust*. This is why it was instructive to begin this Part with an etymological analysis.

B *The Nature of a Fiduciary*

In the ordinary course of things, a fiduciary relationship arises when a person (the fiduciary) undertakes to act in another's best interests, or is obliged so to act, and that other reposes confidence in the person so to do: *Hospital Products Ltd v United States Surgical Corp* (1984) ('*Hospital Products*'). Confidence may also be deemed (*Whitehouse v Carlton Hotel Pty Ltd*), and its reposition need not amount to a confidential relationship (*Chan v Zacharia*).

It is exceedingly difficult to define in anything but the vaguest generality the circumstances capable of giving rise to a fiduciary relation. To derive from the case law any criteria of universal application is all but impossible. For this reason, scholars (most notably Paul Finn) have described the notion of a fiduciary as a 'concept in search of a principle'. There is some truth to this assertion. The character of a fiduciary is difficult to articulate because of the flexible, ephemeral nature of its treatment by equitable doctrines.

Determining whether a particular relationship is of a fiduciary character is important because certain consequences flow from its existence. These consequences take the form of obligations placed on the fiduciary (ie, the party obliged to act in the other's best interests) over and above any other duties in contract or tort. Breach of a fiduciary duty may give the principal an equitable remedy.

C *Categories of Fiduciary Relationship*

The following section outlines a method for determining whether a fiduciary relationship does (or ought to) exist between two parties. It begins by noting that there are, broadly, three classes or categories of fiduciary relationship:

- **Presumed categories**
  Established circumstances in which fiduciary obligations are deemed to be owed;

- **Factual fiduciaries**
  Novel circumstances in which, on the facts, a fiduciary relationship exists because (*inter alia*) of: an undertaking by the fiduciary, an expression of mutual trust and confidence, vulnerability of a party or a reasonable expectation that the other will act as a fiduciary; and

- **Anomalies**
  Ex post facto rationalisations for imposing remedies for breach of fiduciary duty, sometimes stemming from moral or remedial concerns.

The large number of inconsistent cases makes it impossible to articulate a taxonomy of universal correctness. For this reason, cases falling outside the postulated taxonomy are termed 'anomalies' and are argued to be bad law or, at least, contrary to principle.

These classes of relation are now considered in turn.

1 *Presumed categories*

Fiduciary relationships arise in many contexts between innumerable classes of people. Often they arise because the principal places trust and confidence in the fiduciary. Because of the frequency with which fiduciary relations arise between certain classes of individuals, courts are willing to presume their existence in at least eight established categories.

Several examples of such categories were given by Mason J in *Hospital Products*. These, and others cited by Meagher, Heydon and Leeming, are listed below. The fiduciary is indicated with an asterisk:

(a) Trustee* and beneficiary;
(b) Agent* and principal;
(c) Solicitor* and client;
(d) Employee* and employer;
(e) Director* and company;
(f) Partner* and partner*;
(g) Court-appointed receiver* and creditors; and
(h) Guardian* and ward.

The preceding eight fiducial contexts cover the vast majority of cases. If a case concerns a presumed category, it will normally be sufficient to argue by assertion that 'this relationship is clearly of a fiduciary character' and move on to deal with issues of scope or remedies. The existence of a fiduciary relationship will be presumed and the relevant party will be deemed a fiduciary.

If such a presumed fiduciary seeks to avoid liability for breach of duty, he or she must make an argument about scope. Specifically, he or she must argue that the conduct of which the plaintiff complains falls outside the scope of his or her duty so that — even though the fiduciary owes obligations in respect of certain, relevant conduct — those duties do not extend to the impugned conduct. Foundational to this argument is that if a certain activity goes beyond the scope or ambit of the relationship, no fiduciary obligations will be owed in relation to it, even though the same parties are involved. There is, in such a case, no relevant duty to breach.

The most common example of a scope argument in the context of an established category is that of the lawyer who expresses his predictions about who will win an upcoming horserace meeting to a client at a party. Clearly, such a lawyer owes fiduciary duties to their client. However, the circumstances in which the 'advice' is given, and the content of that advice, fall outside the normal scope of that lawyer's duty to their client. Gambling advice is, after all, hardly similar (though perhaps not *absolutely* dissimilar) to legal advice! In such a case, the lawyer's conduct at the party is said to fall *outside* the scope of their fiduciary obligations so that no breach can occur, regardless of how incorrect the predictions turn out to be, how negligently they were made, or how dubious the lawyer's motivation for making them (for example, if he owned a share in the 'favourite' horse).

Seven of the eight presumed categories may be described as 'vertical' relationships in that one party — the fiduciary — is in a position of power vis-à-vis the other — the principal — and that only the more powerful party owes duties to the weaker. Typically, this will be due to an imbalance in knowledge (lawyer–client), power (agent–principal), or capability (guardian–ward).

The exception to these 'vertical' relationships is that of partner–partner. The relationship between partners to an enterprise is horizontal, in that they are in roughly equal positions. The effect of this is that fiduciary obligations are owed *both ways*. Each partner is a fiduciary, and each partner owes fiduciary obligations to all other partners. Correspondingly, each party is a principal, and is owed such obligations by the others.

Note that the following categories are not fiduciary relationships in a strict sense, but are instead relationships of presumed undue influence:

- Priest* and penitent (*Brunninghausen v Glavanics*); and
- Parent* and child (*Brunninghausen v Glavanics*).

2 *Factual fiduciaries*

Importantly, the categories of fiduciary relationship are not closed: *LAC Minerals Ltd v International Corona Resources Ltd* (1989) per Sopinka J ('*LAC Minerals*'). This means that a fiduciary relationship may yet arise in circumstances other than those listed above. Indeed, somewhat unsurprisingly, most appellate cases concern novel situations of this type.

Looking at the above relationships, it is possible to discern several attributes common to the 'vertical' categories of presumed fiduciary relationship:

- First, 'that the fiduciary undertakes or agrees to act for or on behalf of or in the interests of that other person in a legal or practical sense';[1]
- Second, that the fiduciary is in a position of power vis-à-vis the other;
- Third, that the other party is correspondingly vulnerable to abuse by the fiduciary of his position; and
- Fourth, that the fiduciary acts in a 'representative' character, on behalf of the other.

Strictly speaking, no single factor is necessary or sufficient. However, in the vast majority of recognised relationships at least one of these attributes will accurately describe the relationship. Thus, although not all of these factors will be required in every case, and although none is

[1] *Hospital Products* (1984) 156 CLR 41, 96–7 (Mason J).

determinative on its own, it can be stated as a general proposition that a relationship is *more likely* to be considered fiduciary if it embodies elements of:

- Undertaking;
- Power;
- Vulnerability; or
- Representation.

The chief issue in cases involving a novel category of relationship is which, if any, of these factors is to be determinative of the existence of a fiduciary relationship. Broadly, the Canadian authorities prefer an approach premised upon vulnerability and power. By contrast, Australian authorities adopt a narrower undertaking or representation test, which operates on a narrowly confined range of 'legal or practical' interests. (Thus it is that almost all of the recognised circumstances in which fiduciary obligations are owed are commercial or involve tangible, material interests.)

Newer Australian cases begin a novel enquiry by asking whether conduct capable of breaching a duty has occurred, and whether any cognisable interest exists or has been lost to the plaintiff. Only then will a court consider whether the nature of that duty is fiduciary. This approach has been described as a kind of 'backwards reasoning'.

Because of the uncertainty associated with novel categories, and the relatively narrow Australian rationale, it is very difficult to succeed by arguing for a novel factual fiduciary relationship. However, in each of the following relationships a fiduciary duty has been deemed to exist:

(a) Bailee* and bailor (*Hospital Products*);
(b) Pawnor* and pawnee (*Mathew v TM Sutton Ltd*);
(c) Life tenant* and remainderman (*Hospital Products*);
(d) Doctor* and patient (*Norberg v Wynrib*, though not always: *Breen v Williams*);
(e) Financial adviser* and customer (*Commonwealth Bank of Australia v Smith*); and
(f) Statutory powers affecting the rights or interests of individuals (*Wik Peoples v Queensland* per Brennan CJ).

It is critical to note, however, that these are not fixed categories and cannot be treated as extensions to the traditional (closed) classes of relationship. Whether a factual fiduciary relationship depends — as its name suggests — upon the precise factual circumstances of the case. Although the relevant factors and general approach adopted in these cases may prove instructive in the assessment of a later case, the fact that a fiduciary relationship was once held to exist can hardly be determinative in another, potentially different situation.

3 *Anomalies*

Anomalous cases arise when judges impose fiduciary duties on a party not meeting any of the established criteria. This may be more or less overt, and may be used to impose or to deny the existence of duties, depending upon the extraneous considerations influencing the enquiry.

That a case is anomalous is normally given away by artificial or incoherent factual analysis. Courts attempting to rationalise the imposition of duties will often misconstrue or mislabel the nature of a party's relationship with another, or ignore the fundamental nature or objectives of that person, entity or their associated transaction (see, eg, *Chase Manhattan Bank v Israel–British Bank*, positing that the defendant bank owes a fiduciary duty to the plaintiff bank). The motivation for doing so is normally remedial: a finding that a fiduciary relationship exists opens the door to a whole new panoply of remedies with which to vindicate a needy plaintiff.

Equally erroneous, I submit, is the situation in which a court demands satisfaction of arbitrary property requirements — as where a relevant 'interest' is required to have been lost before equity's intervention will even be contemplated. Important non-pecuniary aspects of a party's role in a relationship may be ignored in favour of purely economic considerations (see, eg, *Breen v Williams*, though hardly an 'anomaly').

Such cases are most *unfortunate*.

D *Why Are Fiduciary Relationships Important?*

The naïve preliminary question might well be asked: why is it so important to characterise a relationship as fiduciary? More generally, why are many plaintiffs so keen to allege breach of fiduciary duty? There are two main answers to these questions.

1 *Remedial advantages*

The first is remedial in nature. Plaintiffs often argue for a fiduciary relationship because, if breached, they will be entitled a wider range of remedies. A plaintiff may want more than mere damages — for example, they may want to obtain control of the defendant's business or be entitled to their profits (which may be substantially higher than their own losses occasioned by the breach). Both of these remedies are potentially available to plaintiffs who successfully establish breach of fiduciary duty; however, they are generally not available otherwise. (There is no entitlement as of right; the award is discretionary.)

The availability of these additional remedies is particularly important when the defendant is insolvent, since many remedies for breaches of fiduciary duty are proprietary. Proprietary remedies ensure victory for the successful plaintiff in a subsequent priority dispute with the defendant's unsecured creditors.

2 *Higher standards of conduct*

Fiduciary obligations are among the strictest known to law. Because of the substantial weight of policy underpinning their existence, they are likely to be construed broadly and favourably to the principal. Indeed, if fiduciary obligations were to be placed in a 'hierarchy of propriety' among the other duties known to law, they would be appear at the apex:

- Fiduciaries;
- Persons with knowledge of a special vulnerability;
- Persons in a position of trust and confidence;
- Persons bound to act in good faith;
- Contracting parties; then
- Strangers owing a duty of care.

Consequently, it will probably be easier for a plaintiff to allege that a fiduciary obligation has been breached (assuming one exists) than to allege breach of contract or tort. This is because fiduciary law imposes higher standards of conduct upon fiduciaries than the common law does upon promisors and tortfeasors. What this higher standard means is that a party may be liable in equity for conduct that at common law would not be regarded as tortious or in breach of contract.

II *Novel Fiduciary Relationships*

A *General Principles*

The following section considers factors relevant to the determination of novel or factual fiduciary relationships. Several Australian examples are considered, and the broader Canadian approach examined by way of contrast.

In *LAC Minerals*, a Canadian case, Sopinka J identified several factors said to indicate the existence of a fiduciary relationship. These included:

- '[R]elationships of trust and confidence or confidential relations' (though actual trust and confidence is unnecessary: *Hospital Products* per Gibbs CJ);
- 'Exercise of a power or discretion which will affect the interests of [an]other person in a legal or practical sense', though again this is unnecessary;
- Vulnerability of the other party 'to abuse by the fiduciary of his position', which is, correspondingly, not required in all cases (*C-Shirt Pty Ltd v Barnett Marketing and Management Pty Ltd* per Lehane J);
- That the parties expect the alleged fiduciary to act like one (*Glandon Pty Ltd v Strata Consolidated Pty Ltd*); and
- If the alleged fiduciary holds some kind of power or authority, the purpose for which they hold it ('the touchstone of fiduciary obligation … the fundamental question' per Lehane J).

As will be observed, these factors are far from necessary constituents of a fiduciary relationship. However, in general, the fact that a person is bestowed powers or authority *for the purpose of* serving exclusively the interests of another strongly suggests that they are in a fiduciary relationship with that other.

***Hospital Products Ltd v United States Surgical Corporation* (1984) HCA:**

<u>Facts</u>

- It will not come as a surprise that the first respondent ('USSC') manufactures surgical equipment in the United States
- USSC appoints Blackman as its exclusive Australian distributor from 1 April 1979
- HPI is controlled by a Mr Blackman, who also manages the appellant ('HPL') companies
- HPI acquires USSC's demonstration products, sterilises and begins promoting them in accordance with the distributorship agreement
- HPI begins taking orders for USSC products; however, it defers sending the orders, which begin to accumulate
- In the meanwhile, Blackman is developing the capacity to manufacture surgical equipment locally, and is amassing an interested client base of unfulfilled orders
- USSC is not aware of this, and eventually terminates the distributorship agreement
- HPI, having finalised its own manufacturing arrangements, now fulfils the pre-existing orders from its own stock and begins to compete with USSC in the field of surgical products in Australia
- HPI also executes a reverse takeover of HPL (stripping HPI of its assets)
- USSC commences proceedings against HPI, HPL and Blackman
- USSC alleges a fiduciary relationship so that it can be entitled to the powerful equitable remedies that come from breach of fiduciary duty
    - Although discretionary, a remedial constructive trust could be alleged over all of HPL's (and thus HPI's) assets

- Equitable liens and charges could also be issued
- These remedies are more secure against insolvent defendants
  - Obtaining a proprietary remedy like this is especially important where the defendant is of limited solvency
  - A proprietary right gives USSC 'first bite' of HPL's assets as against its other creditors
- The standard of conduct expected of fiduciaries is higher than contracting parties
  - Equity treats fiduciary relationships as at the top of the 'hierarchy of propriety' — so even a slight anomaly could amount to breach
  - It is therefore easier to allege breach of fiduciary duty than breach of contract against HPL — assuming that such a relationship exists

<u>Issue</u>

- Was there a fiduciary relationship between USSC and HPI, or between USSC and Blackman?
- If so, did HPI's conduct, through Blackman, place it in breach of the fiduciary duty it owed to USSC?
- That being the case, to what remedy is USSC entitled from HPL?

<u>Reasoning</u>

- Supreme Court: yes, breaches of fiduciary obligations to be remedied by an account of profits, in turn secured by an equitable lien over HPI's assets (McLelland J)
  - This made USSC a secured creditor of HPI, such that if HPI went bankrupt, USSC would receive first entitlement to HPI's assets

- Court of Appeal: HPL was constructive trustee over all the assets it acquired in the takeover from HPI because it acquired them with notice of USSC's business and goodwill
  - This is a much broader remedy for USSC
  - This granted USSC complete control over HPL, allowing it to either halt its operations, or to take them over and run them itself (in equity, USSC is now the owner)

- High Court:
  - Mason J: emphasises undertaking and representations of the fiduciary (more prevalent in Australia: reflects a constricted notion of fiduciary relationships)
  - Dawson J: emphasises vulnerability of the principal and power of the fiduciary (popular in Canada: expansive view of fiduciary relationships)
  - Most judges oscillate between these approaches
  - No breach of fiduciary duty (majority)
  - Just breach of contract

- Gibbs CJ:
  - The fact that the principal subjectively trusted the fiduciary is neither necessary nor sufficient for the existence of a fiduciary relationship
    - Likewise for inequality of bargaining power
  - HPI did not become a fiduciary in respect of USSC's goodwill, despite being entrusted with its protection in Australia
    - The fact that there is a duty to be performed under a contract cannot in every case create a fiduciary obligation
    - Contractual duties under ordinary commercial contracts will not of themselves create fiduciary obligations
  - The relationship between the parties was not a fiduciary one
    - Although USSC relied on HPI to promote its products and so had power to affect USSC's interests, two features 'together constitute an

insuperable obstacle' to accepting that HPI was a fiduciary:
    - First, the arrangement was commercial
        - Thus, the parties were free to include terms to protect their position (no vulnerability)
        - The transaction was conducted at arms length and on an equal footing (no inequality)
        - USSC itself prepared the distributorship agreement with its in-house counsel
        - Even as a result of fraud, an ordinary commercial contract made in those circumstances is unlikely to give rise to fiduciary obligations
    - Second, USSC knew that HPI should make profit from the arrangement — indeed, this was the whole point of the transaction
        - A conflict between the interests of HPI and USSC was likely to arise
        - Any such conflict was not necessarily to be resolved in favour of USSC
        - 'How, in those circumstances, is it possible to say that HPI was under an obligation not to profit from its position, and not to place itself in a situation in which its duty and its interest might conflict?'
  - On the facts, HPI was entitled to profit and the transaction was a commercial and contractually (rather than equitably) regulated one
    - The extent of HPI's obligations was 'to act reasonably' — this falls short of creating fiduciary obligations
    - To give an equitable remedy would be to remedy 'gross breach of contract' and 'a fraudulent course of conduct' with equitable sanctions
        - This would be to commit the fusion fallacy
    - Commercial morality is 'vindicate[d]' by the fact that ordinary common law remedies (damages for fraud, breach of contract) are available and are sufficient
  - Conclusion: HPI did not stand in a fiduciary position vis-à-vis USSC

- Wilson J: agrees with Gibbs CJ

- Dawson J:
  - Underlying all cases is that, inherent in the fiduciary relationship, is a position of disadvantage or vulnerability on the part of one party which causes them to place reliance on the other such as to demand the protection of equity
  - On the facts, the commercial, arms length nature of the relationship takes it outside the ambit of fiduciary law
  - Agrees with Gibbs CJ

- Mason J (dissenting):
  - Emphasises HPI's undertaking to act for USSC
    - There is a representative element to the fiduciary relationship
    - 'A 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'
    - This gives the fiduciary a special opportunity to act in a way that causes harm to the principal
    - On the facts, all these elements were present: Blackman and HPI undertook to distribute USSC's product and promote its goodwill
  - Existence of a fiduciary relationship between HPI and USSC

- Distributor–manufacturer is not an established fiduciary relationship
- Contractual and fiduciary relationships may coexist
- On any reasonable construction of the contract, HPI was at liberty to make some business decisions by reference to its own interests without subordinating those interests to the promotion of the market for USSC's products (so long as HPI did not deliberately do anything to injure that market)
  - Consequently, no comprehensive fiduciary relationship existed (ie, with respect to the whole enterprise)
  - However, there might still be an obligation to act in another's interests, even if the potential fiduciary is entitled to act in its own interests sometimes
- The reluctance to subject commercial transactions to equitable doctrines is understandable, but simplistic and superficial: commercial transactions should not stand outside the fiduciary regime because, in principle, they create relationships analogous to recognised categories
- HPI was a fiduciary in protecting USSC's Australian product goodwill
  - HPI was entrusted with responsibility for promoting and protecting the market for USSC's products in Australia
  - HPI procured, sold and supplied USSC's products to Australian consumers
  - HPI was therefore acting in both USSC's interests and its own
    - Simply being entitled to act in one's own interests is not an answer to a suggestion of a fiduciary relationship if there is *also* an obligation to act in the interests of another
  - HPI enhanced both USSC's local product goodwill and that of its own distributorship
  - HPI was obliged not to compete or to injure USSC's market
  - HPI was entitled to prefer its own interests in situations where they would come into conflict with USSC's, but it was still required by the contract to act in good faith, and could never act solely in its own interests
    - This is more than merely having to act in good faith
    - It was positively obliged not to injure USSC's market or to compete
    - It was positively obliged to pursue marketing activities
  - Commercial relationships do not stand outside the fiduciary regime
    - However, the duties of a fiduciary can vary with the circumstances of the relationship
    - Eg, no profit rule: becomes 'no profit without agreement'
  - 'This, as it seems to me, fixed HPI with the character of a fiduciary in relation to those activities mentioned, notwithstanding that in pursuing them HPI was also acting in its own interests and that it was carrying on the distributorship business generally for its own benefit and in no sense as a trustee for USSC'

- Scope of the fiduciary duty extends to not profiting without informed consent
  - The scope of the fiduciary duty must be 'moulded according to the nature of the relationship and the facts of the case': *Boardman v Phipps*
  - HPI was under a duty not to profit by virtue of its position as distributor without USSC's informed consent

- HPI was also obliged not to act in a way that created a 'real sensible possibility of conflict' between its interests and those of USSC: *Queensland Mines Ltd v Hudson*
- HPI was under an obligation not to promote its personal interest by pursuing a gain in circumstances in where there is at least a substantial possibility of a conflict between those interests and USSC's

- Breach of fiduciary duty occurred
  - HPI breached its fiduciary duty by taking actions during the term of the distributorship with a view to appropriating USSC's market for itself
  - Specifically, HPI:
    - Secretly developed a capacity to manufacture copies of USSC's products with that intention; and
    - Deferred fulfilment of USSC orders in anticipation of filling those orders with its own competing products
  - Neither breach constitutes the making of a gain; rather, the pursuit of a gain (appropriation of goodwill), which is sufficient
  - USSC did not knowingly consent to this gain (they didn't know about either of these activities)
  - Had USSC found out in time, the beaches could have been restrained by injunction: *Re Thomson*

- Relief for breach of fiduciary duty
  - The fiduciary cannot be permitted to retain the benefit obtained by reason of his breach of fiduciary duty
  - The fiduciary is liable to account for profit obtained in circumstances of conflict or by reason of opportunities or knowledge afforded by the fiduciary position
  - Such profit is held on constructive trust for the principal: this is the mechanism for making the fiduciary account for his gain
  - To determine whether it is appropriate to grant relief by way of constructive trust, ask:
    - (1) What is the breach of fiduciary duty?
    - (2) What is the benefit obtained by the fiduciary as a result?
  - Here, HPI's benefit was the profits it made in the 'headstart' period ending November 1980 (USSC was not then distributing products)
    - The benefit was *not* the assets of HPI, as the Court of Appeal determined
    - Such a benefit would be too wide-ranging, going beyond both the fiduciary relationship and depending on the view that HPL was fraudulently established
  - HPI did not obtain goodwill as a benefit, because it stopped selling its products on the market shortly thereafter
  - (It is assumed that this returned to USSC, and not other competitors)
  - For the same reason, no constructive trust arising from fraud can be imposed over the goodwill (and thus HPL's assets): it was not a gain made by HPI

- Deane J:
  - USSC is entitled to an order that HPI account, as constructive trustee, for any profit it derived from distributing its competing products in Australia until November 1980, when it ceased distributing same
  - The account of profits is secured by an equitable lien over HPL's assets
  - However, the basis for this remedy differs from that utilised by Mason J

- No fiduciary relationship exists between HPI and USSC in respect of goodwill
- The constructive trust should instead be viewed as equitable relief 'appropriate to the particular circumstances of the case[,] rather than as arising from a breach of some fiduciary duty flowing from an identified fiduciary relationship'
- The remedy is available on unjust enrichment grounds — regardless of whether there was a breach of fiduciary duties
  - This doctrine straddles both equity and the common law
  - It occasionally surfaces in the case law, but is not the orthodox position
  - Deane J is effectively granting an equitable remedy for a breach of contract action
  - Equity should be flexible enough to grant proprietary remedies for deliberate breach of contract
    - [Should it matter whether the breach is deliberate?]
  - [This is arguably a better approach than artificially deeming a fiduciary relationship to exist (which distorts the principles), but may be criticised for its apparent backwards reasoning]
- HPI calculatedly breached its contractual obligations to USSC, but these were of a contractual, and not a fiduciary nature
- It would therefore be unconscionable ('not in good conscience') for HPI to retain the benefit of this appropriation in breach of its contractual (or, in any event, equitable) obligations to USSC
- In the result, equity imposes a constructive trust as the appropriate form of relief to prevent such unconscionability

<u>Decision</u>

- (5:0) HPI was in breach of contract to USSC
- (4:1) HPI was not in a fiduciary relationship with USSC, so there was no right to equitable relief (Mason J dissenting)
- Mason and Deane JJ: the equitable relief should be an account of profits (as McLelland J proposed), rather than a constructive trust (Court of Appeal)

After the *Hospital Products* decision, the unsuccessful defendant, Hospital Products Ltd, began to move its assets offshore ('an unscrupulous and hyperactive defendant'). See also *Ballabill Holdings v Hospital Products Ltd* (1985), where the New South Wales Court of Appeal imposed a *Mareva* injunction, freezing the assets of Hospital Products. (Had a constructive trust order been made, this would have happened automatically.) This illustrates the importance of considering the enforceability of a court order — even one of the High Court — and the relative susceptibility of damages orders to subversion by an unruly defendant.

In subsequent cases, the approach of Mason J has been favoured in Australia. However, Deane J's judgment has been noted with approval by the House of Lords in *Attorney–General v Blake* (2001). The British government there sought an account of profits over sales of a controversial memoir by an escaped treasonist and former MI5 spy. The Court held that there was no liability for breach of confidence (all of Blake's stories were public knowledge) or breach of fiduciary duty (no relationship continued to exist between MI5 and Blake beyond the term of his employment), but he had deliberately and calculatedly breached his employment contract with MI5. The remedy was an account of profits, and the Court was strongly influenced by Deane J's 'discretionary remedialism'. However, this is not good law in Australia: a proprietary remedy such as account of profits will only be imposed for breach of fiduciary duty. 'The fiduciary relationship is the key that unlocks the door to proprietary remedies.'

On the facts of *Hospital Products*, the remedy granted to USSC in the High Court would probably have proven insufficient. If HPL declared bankruptcy, the trustee in bankruptcy would realise

HPL's assets and distribute the remainder among the creditors accordingly. This might mean that individual creditors receive only a fraction of their entitlement. However, a secured creditor is entitled to the whole of their secured interest before any of the other creditors, unless there is another secured creditor who has a better interest (eg, a legal right rather than an equitable lien, or, in general, a prior equitable right).

If the unsuccessful defendant refuses to pay, the plaintiff can obtain an order of seizure and distress. Then, in execution proceedings, the sheriff will go in and seize assets to the value of the claim. Thus, the importance of a proprietary remedy is that these additional mechanisms can be avoided; this saves legal costs, results in a larger remedy, and makes it easier to obtain and enforce by the plaintiff.

B *Partnerships and Joint Ventures*

Justice Mason's 'undertaking' test from *Hospital Products* is now ordinarily applied by Australian courts to determine whether a fiduciary relationship exists in the context of a vertical relationship. However, partnerships and other horizontal relations are ill-suited to application of this test. Consequently, a different test applies. To apply the correct test, it must first be determined whether a partnership exists.

1 *Is there a partnership?*

A partnership consists of two or more people who pursue an activity in common with a view to making a profit. Partnerships — whether personal, professional or commercial — are of a fiduciary character, but cannot easily be characterised as cases where one partner agrees to act for another. More commonly, all partners agree to act for all others, so that each person owes reciprocal duties.

Partnerships are to be distinguished from other fiduciary relationships, but include joint ventures. See, for example, *News Ltd v Australian Rugby League* (1996), where the Full Court of the Federal Court of Australia determined that clubs of the ruby league did not owe one another fiduciary duties since they existed for the pursuit of self-interested purposes and not in partnership with one another.

In that case, Gummow J identified two forms of business relationships: vertical and horizontal. Vertical relationships are characterised by an imbalance of power; the *Hospital Products* test should be applied. By contrast, the horizontal business relationship involves two or more parties of roughly equal strength. All parties are working towards the same common goal.

Preliminary step: identify the kind of business structure involved in order to apply the correct test for the existence of a fiduciary relationship.

Factors suggesting that a partnership exists:

- All parties are acting for all others;
- All parties are pursuing the same common interest, and not individual purposes;
- There is a common goal;
- The parties are of roughly equal strength.

Whether an arrangement is a partnership is a matter of substance not form. Thus, the fact that parties describe their enterprise as a 'joint venture' rather than a partnership will not be determinative if the substance of the relationship is to create a partnership (*United Dominions Corp Ltd v Brian Pty Ltd*).

2 *Test for existence of fiduciary duty between partners*

In *News Ltd v Australian Rugby League*, Gummow J applied *United Dominions Corp Ltd v Brian Pty Ltd*, which held that a separate test is applied to horizontal relationships. Specifically, to determine whether a fiduciary relationship exists, it must be asked:

Does a high degree of mutual trust and confidence exist between the parties?

On the facts of *News Ltd v Australian Rugby League*, no such degree of trust existed between the clubs, which were in competition for sponsorship and players, so no fiduciary relationship existed.

3 *Current authority for partnerships*

Having established that a partnership exists, the circumstances will give rise to fiduciary duties among the partners if they repose a high degree of mutual trust and confidence in one another. Trust and confidence may be inferred from the existence of deposits into a joint venture that are unprotected by a contractual mechanism, but whether it exists will ultimately depend on the facts (*United Dominions Corp Ltd v Brian Pty Ltd*).

United Dominions Corp Ltd v Brian Pty Ltd **(1985) HCA:**

Facts
- Brian, SPL and UDC enter into a joint venture to build a shopping centre
- The centre is built and becomes profitable; however, Brian does not receive any profits
- When Brian enquires why, he is told that UDC will first be paid moneys owing to it under a commercialisation clause, hitherto unknown, in the contract between UDC and SPL before any money is paid out to the other investors
- UDC had created legal mortgages over the shopping centre; the only way Brian could override these rights would be if it was owed fiduciary duties by UDC, since the impact of the third party proprietary rights and covenants would be nullified
- Brian argues that because the standard of conduct required of parties to a fiduciary relationship is significantly higher than that required of contracting parties, UDC should have made full disclosure of the collateralisation clause (even though UDC was not required to do so as offeror)

Issues
- Form and substance: can the self-described 'joint venture' amount to a partnership in equity despite being labelled otherwise?
  - UDC argued that the relationship was not fiduciary because it was not described as a partnership in the agreement
- What is the test to be applied for partnership agreements?
- Are pre-contractual negotiations capable of giving rise to fiduciary obligations?

Reasoning
- In substance, the agreement created a partnership
  - Whether a relationship is fiduciary is not dependent on the label the parties attach to it
  - It is a question of the substance of the agreement
  - If the arrangement is found to be fiduciary, a fiduciary character it shall retain, regardless of the language of the parties

    - However, if the parties explicitly agree that the relationship is not fiduciary, or that certain fiduciary obligations do not apply, then this will be recognised and enforced

- The test of fiduciary status for any partnership or joint venture is whether a high degree of mutual trust and confidence exists between the parties
    - Here, placing money into a joint venture entails a high degree of trust and confidence
    - There was therefore a high degree of mutual trust and confidence
    - This is a fact-dependant analysis

- Pre-contractual negotiations can (though will not always) constitute a fiduciary relation
    - Brian paid money into the joint venture prior to signing the joint venture agreement
    - A fiduciary relationship can exist during the negotiation period leading up to the formation of the agreement
    - The fact that Brian paid this money without contractual protection indicates the existence of a high degree of mutual trust and confidence, suggesting that they were in a fiduciary relationship

Decision

- The relationship between the parties is fiduciary
- SPL and UDC have acted in breach of duty by agreeing on the collateralisation clause

4 *Pre-contractual relationships between possible parties to a joint venture*

Issue: can fiduciary obligations be imposed on parties negotiating towards a joint venture, despite not reaching agreement at the time of the alleged breach?

In *LAC Minerals v International Corona Resources*, a minority of the Canadian Supreme Court found a fiduciary relationship between two companies engaged in unsuccessful joint venture negotiations, one party having exposed itself to vulnerability by revealing confidential information to the other. The minority would have imposed a remedy of constructive trust.

LAC Minerals v International Corona Resources **(1989) Canada SC:**

Facts

- Corona, a small mining company, owns the rights to exploit certain land
- Corona conducts geological surveys of the land
- Corona does not have the resources to develop a mine capable of exploiting that land
- Consequently, they enter into negotiations with a larger company, LAC, in order to negotiate a joint venture mining operation
- Corona reveals the results of their geological surveys to LAC
- Examining the surveys reveals to LAC's geologists that there are substantial gold deposits on the neighbouring property, owned by Mrs Williams (an elderly woman unaware of the resources under her land)
- The joint venture arrangement does not proceed; however, when Corona subsequently tries to obtain mining rights to the neighbouring land, LAC makes a higher competing bid and purchases Mrs Williams' property
- LAC proceeds to make some $700m from the mine, which is among the most successful in Canada

Issue

- Did LAC's misuse of Corona's confidential information amount to breach of confidence?
- Alternatively, was there a fiduciary relationship between Corona and LAC, despite there not being any concluded joint venture agreement?
    - What is the relevant test for a fiduciary relationship?
    - Did the negotiations themselves create a fiduciary relationship?
- If so, was LAC's entry of a competing bid a breach of their fiduciary duties to Corona?

Reasoning

- What is a fiduciary?
    - Wilson J: focuses on vulnerability
        - Ordinarily, there is no fiduciary relationship between two negotiators to a joint venture engaged in arms-length negotiations
        - However, it is possible for such a relationship to arise by virtue of the conduct of the parties
        - Here, a fiduciary relationship arose when Corona made available to LAC its confidential information, thereby placing itself in a position of vulnerability to LAC's misuse of that information
        - This is an approach similar to Dawson J in Australia

    - La Forest J: vulnerability relevant but not decisive
        - The term 'fiduciary' is used in at least three distinct ways
            - First way: presumed relationships
                - 'The focus is on the identification of relationships in which, because of their inherent purpose or their presumed factual or legal incidents, the courts will impose a fiduciary obligation on one party to act or refrain from acting in a certain way'
                - 'The presumption that a fiduciary obligation will be owed in the context of such a relationship is not irrebuttable, but a strong presumption will exist that such an obligation is present'
                - 'It is only in relation to breaches of the specific obligations imposed because the relationship is one characterised as fiduciary that a claim for breach of fiduciary duty can be founded'
            - Second way: factual categories
                - 'Corona's contention is not that "parties negotiating towards a joint-venture" constitute a category of relationship, proof of which will give rise to a presumption of fiduciary obligation, but rather that a fiduciary relationship arises out of the particular circumstances of this case'
                - 'The imposition of fiduciary obligations is not limited to those relationships in which a presumption of such an obligation arises. Rather, a fiduciary obligation can arise as a matter of fact out of the specific circumstances of a relationship. As such it can arise between parties in a relationship in which fiduciary obligations would not normally be expected.'
                - 'What must be shown, in [Professor Finn's] view, is that the actual circumstances of a relationship are such that one party is entitled to expect that the other will act in his

interests in and for the purposes of the relationship.'
      - 'The critical matter in the end is the role that the alleged fiduciary has, or should be taken to have, in the relationship.'
      - 'It is in this sense, then, that the existence of a fiduciary obligation can be said to be a question of fact to be determined by examining the specific facts and circumstances surrounding each relationship'
    - Third usage: remedial anomalies
      - Courts use fiduciary language because it makes certain remedies available to a wronged plaintiff
      - 'In this sense, the label fiduciary imposes no obligations, but rather is merely instrumental or facilitative in achieving what appears to be the appropriate result'
      - See, eg, *Chase Manhattan Bank NA v Israel–British Bank (London) Ltd*
      - This approach has been criticised by Professor Birks as 'mov[ing] the characteri[s]ation of a relationship as fiduciary from the reasoning which justifies a conclusion to the conclusion itself: a relationship becomes fiduciary because a legal consequence traditionally associated with that label is generated by the facts in question.'
      - 'In my view, this third use of the term fiduciary, used as a conclusion to justify a result, reads equity backwards. It is a misuse of the term.'
      - To avoid misuse predicated on a desire for remedial flexibility, courts should recognise proprietary remedies such as the constructive trust as available outside of fiduciary relationships
  - On these facts, the most relevant category of fiduciary relationship is the second one: 'whether the facts in this case … support the imposition of a fiduciary obligation within the second category … and whether, acting as it did, LAC was in reach of the obligations thereby imposed'
  - Generally, fiduciary obligations will not attach to commercial transactions
    - However, they can arise in certain circumstances — there is no single test
    - The question whether fiduciary obligations exist 'is a question of fact in each case': *United Dominions Corp Ltd v Brian Pty Ltd*
    - 'LAC urged this Court not to accept [a finding of fiduciary obligations], warning that imposing a fiduciary relationship in a case such as this would give rise to the greatest commercial uncertainty in commercial law, and result in the determination of the rules of commercial conduct on the basis of *ad hoc* moral judgments rather than on the basis of established principles of commercial law'
    - 'Certainty in commercial law is, no doubt, an important value, but it is not the only value'
    - There are already other limitations on commercial conduct, both at law and in equity
    - '[I]t is difficult to see how giving legal recognition to the parties' expectations will throw commercial law into turmoil'
    - 'Commercial relationships will more rarely involve fiduciary obligations. That is not because they are immune from them, but because in most cases, they would not be appropriately

imposed.' (Cites *Hospital Products* per Mason J)
    - 'It is simply not the case that business and accepted morality are mutually exclusive domains'
- Three rationales can be used to justify the characterisation of the relationship between LAC and Corona as fiduciary:
    - Trust and confidence;
    - Industry practice; and
    - Vulnerability
- First, mutual trust and confidence is relevant
    - 'The existence of [a bond of trust and confidence] plays an important role in determining whether one party could reasonably expect the other to act or refrain from acting against the interests of the former'
    - The relationship must be considered as at the time the surveys were handed over to LAC
    - Here, there was such a relationship for two reasons
        - First, because Corona's disclosure of confidential information without other legal protection suggested a relationship of mutual trust and confidence (similar to *Brian*)
        - Second, Corona's practice of disclosure was reasonable in the circumstances because of an established industry practice in the mining industry that negotiations were to be candid and involve sharing of secret information
        - It was expected that Corona would disclose confidential information to LAC, as it was a normal practice in the mining industry (at 36)
    - Thus, it was not unreasonable for Corona to disclose the information to LAC without insisting on confidentiality
        - 'This Court should not deny the existence of a fiduciary obligation simply because the parties could have by means of a confidentiality agreement regulated their affairs'
        - 'I cannot understand why a claim for breach of confidence is available absent a confidentiality agreement, but a claim for breach of fiduciary duty is not'
        - 'Where it is not established that the entering of confidentiality agreements is a common, usual or expected course of action, this court should not presume such a procedure, particularly when the law of fiduciary obligations can operate to protect the reasonable expectations of the parties'
- Second, industry practice is relevant
    - The evidence established that a practice existed that a company in LAC's position 'would not use confidential information derived out of the negotiating relationship in a manner contrary to the interests of Corona'
    - LAC knew of this industry practice
    - '[T]he evidence of experts is of considerable importance in establishing standard practice in the industry from which one can determine the nature of the obligations which will be imposed by law'
    - Industry practice is relevant to the question of 'whether Corona

could reasonably expect that LAC would act or refrain from acting against the interests of Corona'

- Third, vulnerability is relevant: here Corona became vulnerable when it disclosed its confidential information
    - However, vulnerability is not an essential precondition or 'necessary ingredient' in every fiduciary relationship: at 39
    - It is the vulnerability of the class of beneficiaries which should be examined
    - 'Persons are vulnerable if they are susceptible to harm, or open to injury. They are vulnerable if at the hands of the fiduciary if the fiduciary is the one who can inflict that harm.'
    - Fiduciary obligations can still be breached without harming the beneficiary (principal): *Keech v Sandford*
    - Because harm is unnecessary, 'vulnerability or its absence' will not be determinative of the fiduciary question
    - Instead, 'the issue should be whether, having regard to all the facts and circumstances, one party stands in relation to another such that it could reasonably be expected that that other would act or refrain from acting in a way contrary to the interests of that other'
- Application:
    - Corona gave LAC the ability to harm its interests by disclosing confidential information about the property and Corona's intentions
    - Corona's vulnerability is evidenced by:
        - The circumstances in which LAC acquired Mrs Williams' property (LAC could make a better offer)
        - Its junior status and smaller size relative to LAC
        - Its need for LAC's financial support (indeed, the very reason why it contacted LAC to begin with)

- Sopinka J (majority, dissenting in part)
    - The fiduciary relationship is a 'blunt tool of equity'
    - '[N]o ironclad formula supplies the answer' to a novel category of relationship: the court must consider 'what are the essential ingredients of a fiduciary relation and are they present?'
    - However, certain characteristics are so common that 'they serve as a rough and ready guide'
        - 'The fiduciary has scope for the exercise of some discretion or power
        - The fiduciary can unilaterally exercise that power or discretion so as to affect eh beneficiary's legal or practical interests
        - The beneficiary is peculiarly vulnerable to or at the mercy of the fiduciary holding the discretion or power'
        - *Framer v Smith* per Wilson J (dissenting)
    - Vulnerability, or its absence, will conclude the issue of fiduciary obligation
        - Mutual trust and confidence, or undertaking, are not relevant
        - Instead, follows Dawson J in *Hospital Products*
            - 'inherent in the nature of the relationship itself is a position of disadvantage or vulnerability on the part of one of the parties which causes him to place reliance upon the other and requires the protection of equity acting upon the conscience of that other.'

        - Here, there was insufficient vulnerability on Corona's part because they were not economically vulnerable to the actions of LAC
            - Both parties, as mining companies, have access to geologists, engineers and lawyers
            - It cannot be said that one company was more vulnerable than the other
            - The fact that one party (Corona) approached the other (LAC) is irrelevant: in every commercial venture, one party approaches another; this is 'not an *indicium* of a fiduciary relationship'
            - 'The practice among geologists to act honourably towards each other is no doubt admirable and a practice to be fostered, but it should not b used to create a fiduciary relationship where one does not exist'
            - 'If Corona placed itself in a vulnerable position because L[AC] was given confidential information, then this dependency was gratuitously incurred. Nothing prevented Corona from exacting an undertaking from L[AC] that it would not acquire the Williams property unilaterally.'
            - 'Accordingly, if Corona gave up confidential information, it did so without obtaining any contractual protection which was available to it. This and the fact that misuse of confidential information is the subject of an alternate remedy strongly militate against the application here of equity's blunt tool'
            - Vulnerability, as a 'vital ingredient', was therefore 'virtually [LAC]king in this case'
        - Nor did the negotiations get as far as they did in *United Dominion Corp v Brian*
            - In *Brian*, all parties knew of the particular joint venture structure
            - The 'arrangements [in *Brian*] between the prospective joint venturers had passed far beyond the stage of mere negotiations'
            - Here, LAC and Corona were still negotiating towards 'a joint venture *or some other* business relationship' (emphasis added)
            - 'The most that can be said is that the parties came to an informal oral understanding as to how each would conduct itself in anticipation of a joint venture *or some other business arrangement*' (emphasis added)
            - They could not yet precisely identify the content of their relationship; certainly, Corona did not say to LAC that they should purchase the Williams property
            - On the facts, neither party had considered what legal structure would be adopted
            - *Brian* can be distinguished on this basis
            - The decision to adopt a legal structure may be the cutting off point for whether the negotiations are themselves fiduciary
        - However, there was a breach of confidence
        - Damages will be awarded, but not a constructive trust

- What is the appropriate remedy?
    - Where the amount of lost profits is uncertain, a constructive trust provides a more flexible measure of actual and future losses than fixed damages
    - Damages may not provide a sufficient deterrent for resourced parties that stand to make a greater gain from breaching the duty and then paying some amount, rather than meeting their obligations
    - The breaching party should not be rewarded for their lapse in duty; damages

might in fact allow them to obtain a net benefit
- Why not an account of profits secured by an equitable lien?
  - This wouldn't give LAC the entirety of the profits (eg, 50 per cent of what the mine produces)
  - This deals with some of the issues, though it still rewards LAC for a proportion of their breach
  - It might also discourage efficient use of the mine
  - Determining a proportion can be fairly arbitrary ('equity is equality'?)
  - If it was a 50/50 proportion, it would effectively amount to a Court-imposed joint venture arrangement, which was the very issue upon which the parties failed to agree
  - It might also be argued that LAC, having taken a substantial risk of its own (and paid for the rights, equipment, *et cetera*), should be entitled to some portion of the profits — on the rationale that the risks taken by the parties should be balanced in some form
  - An accounting is not normally a restitutionary measure of damages (it arguably goes further, since it is measured by the defendant's total gain, rather than that proportion which happened to be at the plaintiff's expense)

- Wilson and La Forest JJ:
  - LAC is to hold the mine on constructive trust for Corona subject to deductions for their expenditure of roughly $58m
  - Effectively, LAC is ordered to transfer the mine to Corona for that amount; this is a very controversial decision
  - Constructive trust is the appropriate remedial vehicle because LAC was unjustly enriched by Corona (since LAC would not have had the mine if they did not misuse the confidential information)
    - A constructive trust is not to be limited to 'situations where a right of property is recognised'
    - To do so 'would limit the constructive trust to its institutional function, and deny to it the status of a remedy, its more important role.'
  - Constructive trust is the only remedy capable of fully compensating Corona
    - There is no restitution to make since Corona never actually owned the Williams property (so it cannot be 'given back')
    - However, restitutionary relief will often be appropriate for breaches of fiduciary duties and breaches of confidence
  - However, it does cause equity to impose an outcome far more profitable to Corona than would have been the case had they successfully entered into a joint venture (pursuant to which there would have been profit sharing according to some ratio); by contrast, Corona is here getting the entire mine, reduced only by LAC's own expenses
  - Wilson J: if the remedy was simply damages, it may not be full compensation because valuation techniques are inherently inaccurate, and may underestimate the amount of gold, the future price of gold, inflation, exchange rates and other externalities
  - Constructive trusts prevent the wrongdoer from profiting *in any way* from their wrongdoing
    - Cf damages (this makes it less likely that a company would 'pay the breach cost' in order to make a greater gain)
    - 'If by breaching an obligation of confidence one party is able to acquire an asset entirely for itself, at the risk of only having to

compensate the other for what the other would have received if a formal relationship between them were concluded, the former would be given a strong incentive to breach the obligation and acquire the asset'
- [Those of the law and economics school of thought might question the validity of this reasoning, perhaps arguing that a court should not make exploitation of a business opportunity less efficient by depriving rational parties of a viable alternative to fulfilling their obligations; I do not agree with that objection]

- Imposing a constructive trust rewards bargaining in good faith by acting as a deterrent to breach
  - It 'strengthens the social fabric [fiduciary] duties are imposed to protect' by setting the standard of conduct high
  - It encourages full and frank disclosure between negotiators
  - It is necessary to maintain commercial morality within the mining industry
  - This makes the negotiating process more efficient by reducing the transaction costs associated with maintaining confidentiality and protecting against improper conduct that wouldn't amount to breach of contract
  - Efficient, fair, better for business, better for society
- But arguably overcompensates; does not do corrective justice between the parties
  - The social ends aimed for by the Court are broader than necessary; they go beyond the parties in the case
  - This goes against the fundamental principle that equity is concerned with justice as between the parties in individual cases
- Should the constructive trust simply compensate, or is it intended as a deterrent, and to uphold wider social and moral standards?
  - 'The moral quality of the defendants' act may also be another consideration in determining whether a proprietary remedy is appropriate. Allowing the defendant to retain a specific asset when it was obtained through conscious wrongdoing may so offend a court that it would deny to the defendant the right to retain the property. This situation will be more rare, since the focus of the inquiry should be upon the … plaintiff … not … the defendant.'
  - Here, a constructive trust is the appropriate remedy:
    - But for LAC's beaches of duty Corona would have acquired the Williams property
    - It is almost impossible to accurately value the property
- The trial judge calculated damages just in case the constructive trust was overturned on appeal: CAD $700m
  - La Forest J: it is impossible to predict the true measure of damages; questions valuation techniques
    - Trial judge: 'There are almost insurmountable difficulties in assessing the value of such a property in the open market'
    - Trial judge: 'The profitability of the mine, and accordingly its value, will depend on the ore reserves of the mine, the future price of gold from time to time, which in turn depends on the rate of exchange between the US dollar and Canadian dollar, inflationary trends, together with myriad other matters, all of which are virtually impossible

to predict.'
- La Forest J: 'To award only a monetary remedy in such circumstances when an alternative remedy is both available and appropriate would, in my view, be unfair and unjust.'
- This is arguably more of a problem in the context of civil damages, especially for future economic loss in the context of personal injury
- A constructive trust is viewed as inherently accurate since it only awards what is earned from the mine — certainly more accurate than an estimate of future damage, but unlike an account of profits it prevents the fiduciary profiting from its wrong
- Property is *sui generis* (unique); the only way to remedy a breach resulting in the loss of property is to provide the wronged party *with* that property

Decision
- Majority (three judges):
  - LAC is liable for breach of confidence (a doctrine comprising both legal and equitable elements) by misusing the confidential information
  - No fiduciary relationship exists between the parties

- Minority (Wilson and La Forest JJ):
  - LAC is liable for breach of fiduciary duty
  - Grant a remedy by way of constructive trust to Corona

C *Financial Advisers*

Issue: can service providers, whose obligations are normally contractual (or tortious), also owe fiduciary obligations to their clients? What is the point at which one kind of duty transforms into the other?

Whether a relationship between a professional adviser and his or her client gives rise to fiduciary duties depends on the particular facts: *Hodgkinson v Simms* (1994).

Commonwealth Bank v Smith (1991) FCA:

Facts
- The Commonwealth Bank had been Smith's adviser and bank for a period of 24 years
- During this time, the Smiths had been engaged in a variety of business activities, including farming and waste removal
- However, their business experience and commercial understanding was limited
- The Smiths decide to undertake a new venture in hospitality: the operation of a hotel
- They decide to obtain the Bank Manager's help in receiving advice about selecting a suitable hotel and advising as to its operation
- The Bank also happened to have other clients who wanted to sell their hotels; these clients owed substantial sums to the Bank
- The Manager is keen to settle up these accounts, so he tells the Smiths that:
  - A particular hotel, the Weeroona Hotel, is a good one;

  - It is better than others on the market;
  - They can afford it; and
  - It is being sold for a good price
- However, he does not tell them that he has received a mortgage valuation for a figure substantially lower than the sale price
  - The Smiths ask him whether it is a good price; he still tells them that it is
- The Bank Manager reveals that he is under a conflict of interest, because the vendors are also his clients
  - However, he says little else about it, and discouraged the Smiths from seeing an accountant or a hotel broker, and instead encouraged them to use the vendor's solicitor for the sale (an attempt to lead them away from independent advice)
- Relying on the Manager's advice, the Smiths purchase the hotel and obtain finance from the Bank
- However, when the Smiths discover that they had been duped, they commence proceedings against the Bank

<u>Issue</u>
- Did a fiduciary relationship between Smith and the Bank, through its manager?

<u>Reasoning</u>
- Where a bank gives financial advice, in addition to the contractual relationship between it and its customers, the relationship might be such as to found either a common law duty of care; or a fiduciary duty; or both
- The Bank will do this where it creates an expectation that it will act and advise its customers what is in their best interests
- The relationship can even arise when the Bank has a commercial interest of its own in lending the customer money
- Trial judge (cited with approval by the Federal Court of Australia at 393–4):
  - 'Even if Mr Dungan had disclosed to the applicants that he was acting for the vendor in … giving particulars of the hotel business he would still have been placed in an impossible position when the applicant sought his advice on the merits of the transaction, and inquired whether they should offer less than the vendor's asking price.

    He could give no answer on these matters without running into conflict with his duty to at least one side in the negotiations. In the circumstances of this case Mr Dungan ought never to have advised the applicants at all on the merits of the transaction. ... He should have explained to them the need to get advice on the questions raised by **[394]** them from someone who is independent. When Mr Smith asked if he should seek accounting advice, he should have been told to do so.'

- '**[392]** The starting points for consideration of the present problem are the findings that Mr Dungan assumed the role of introducing the parties and bringing them together, that he then acted as the respondents' financial adviser in the matter, and that they evinced complete faith in him. The circumstances in which that came about need to be borne in mind. We do not repeat, although it is highly significant here also, what we have already said as to the background of his earlier dealings and discussions with the respondents and as to the type of people which the respondents were. These are important matters to be taken into account in consideration of the question of whether a fiduciary relationship arose.'

  'In our view, the primary judge was correct in concluding on the facts that the bank became the investment adviser of the respondents in the matter of the purchase of the

Weeroona Hotel and that a fiduciary relationship arose. The question then was one of (i) identifying the relevant incidents of that relationship and duties arising from it, and (ii) determining whether there had been a breach of duty leading to loss for which there was an obligation upon the bank to compensate the respondents.'

'The crucial incident of the fiduciary relationship in this case arose from the conflicting interests between the two sets of customers of the bank. As von Doussa J put it, and we agree, Mr Dungan had become the representative of one customer of the bank … in helping to bring about the sale of their business to two other customers of the bank. Not only must the fiduciary avoid, without informed consent, placing himself in a position of conflict between duty and personal interest, but he must eschew conflicting engagements. The reason is that by reason of the multiple engagements, the fiduciary may be unable to discharge adequately the one without conflicting with his obligation in the other. Thus, it has been said, after ample citation of authority, that where an adviser in a sale is also the undisclosed adviser of the purchaser, an actual conflict of duties arises: Finn, *Fiduciary Obligations*, 253–4.'

'In such a case, it is not to the point that the fiduciary himself may not stand to profit from the transaction he brings about between the parties. The prohibition is not against the making of a profit (though many cases of breach of fiduciary duty involve the wrongful acquisition of a profit, rather than the infliction of a loss) but of the avoidance of conflict of duties'

- Here, the relationship was such as to create a fiduciary relationship:
    - Not an arms-length transaction; there was a long history of association — a background of earlier dealings and discussions
    - The 'type of people which the respondents were' — trusting, and evincing complete faith in the Manager — is also relevant
    - They had no independent advice — indeed, there was active discouragement thereof by the Manager
    - The Manager brought the parties together, creating a situation where he was unable to discharge adequately his duties to the one customer without conflicting with his obligation in the other

<u>Decision</u>

- Here the bank committed both a tort (negligence) and breach of fiduciary duty
- Compensation awarded based on:
    - The difference between purchase price and the real value of the property; plus
    - The percentage and amount of interest charged by the Bank to the Smiths for the loan
    - This ensures that the Bank will not profit from granting the full loan; instead, it will pay the inflated price

Because certain adviser relationships may be of a fiduciary character, financial advisers might also owe these duties. However, the extent to which this is true is unclear at present, as there has been no case directly on point. In Canada, however, the issue has been considered in greater detail.

In *Hodgkinson v Simms*, a majority of the Canadian Supreme Court held that financial advisers will owe fiduciary duties to their clients where it is reasonable for the advisee to expect that the adviser is exercising his or her special skills in their best interests, unless the contrary is disclosed. This determination will be made having regard to the extent of the advisee's trust in the adviser, the confidentiality of the transaction, the complexity and importance of the subject matter, and the extent to which the advisee has reasonably relied on the adviser's recommendations. The advisee must be relying on the skill and knowledge and advice of the adviser. In short:

> *The relationship between an adviser and their client is elevated to a fiduciary level when the client reposes trust and confidence in the broker and relies on the broker's advice in making decisions.*

The minority added that the advisee's vulnerability was also an essential prerequisite, and disagreed with the majority that the plaintiff unreflectively and reflexively followed the advice proffered by his adviser.

Hodgkinson v Simms **(1984) Canada SC:**

<u>Facts</u>

- The plaintiff, a Mr Hodgkinson, seeks advice about tax planning from the defendant, Mr Simms of the accounting firm Simms & Waldman
- The defendant advises the plaintiff to purchase certain property (tax shelter units, so called for their ability to 'shelter' the purchaser's income from taxation)
- The defendant does not disclose that he would receive a referral commission from the property developer of those units
- The plaintiff invests in the units; the defendant receives his commission
- However, the plaintiff's investment suffers when the Canadian market in multi-unit residential buildings collapses
- Hodgkinson commences proceedings against Simms

<u>Issue</u>

- Did a fiduciary relationship exist between Hodgkinson and Simms?

<u>Reasoning</u>

- La Forest J:
    - There is more to a fiduciary relationship than vulnerability
        - Vulnerability is not the hallmark of fiduciary relationships, though it is an important *indicium* of its existence
        - It is 'the "golden thread" that unites such related causes of action as breach of fiduciary duty, undue influence, unconscionability and negligent misrepresentation.'
        - However, as Weinrib notes, '[pre-existing inequality] cannot be the *sine qua non* of a fiduciary obligation that the parties have disparate bargaining strength. … In contrast to notions of conscionability, the fiduciary relation looks to the relative positions of the parties that results from the agreement rather than the relative position that precedes the agreement.'
        - 'In *LAC Minerals*, I … identified three uses of the term fiduciary…'
        - '…outside of the established categories, what is required is evidence of a mutual understanding that one party has relinquished its own self-interest and agreed to act solely on behalf of the other party.'
        - 'More generally, relationships characterised by a unilateral discretion, such as the trustee–beneficiary relationship, are properly understood as simply a species of a broader family of relationships that may be termed "power–dependency" relationships.'
        - However, 'it is simply wrong to focus only on the degree to which a power or discretion to harm another is somehow "unilateral"'
        - 'Further, the relative "degree of vulnerability" … does not depend on

some hypothetical ability to protect one's self from harm, but rather on the nature of the parties' reasonable expectations.'
  - 'Thus in *LAC Minerals*, I felt it perverse to fault Corona for failing to negotiate a confidentiality agreement with LAC in a situation where the well-established practice in the mining industry was such that Corona would have had no reasonable expectation that LAC would use the information to its detriment.'
  - In short, as Lord Scarman recently stated, '[t]here is no substitute in this branch of the law for a meticulous examination of the facts' (*National Westminster Bank plc v Morgan*)

- There is a broad fiduciary duty owed by financial advisers to their clients
  - 'In relation to the advisory context, then, there must be something more than a simple undertaking by one party to provide information and execute orders for the other for a relationship to be enforced as fiduciary.'
  - 'Similarly, the relationship of an investor to his or her discount broker will not likely give rise to a fiduciary duty, where the broker is simply a conduit of information and an order taker. There are, however, other advisory relationships where, because of the presence of elements such as trust, confidentiality, and the complexity and importance of the subject matter, it may be reasonable for the advisee to expect that the advisor is in fact exercising his or her special skills in that other party's best interests, unless the contrary is disclosed.'
  - Advisor–advisee is an example of a power–dependency relationship
  - The concern of Wilson J in *Frame* and Sopinka J in *LAC Minerals* about extending the fiduciary principle to arms length commercial relationships is 'simply not transferable to professional advisory relationships'
  - Keenan J's description of the broker–client relationship in *Varcoe v Sterling* is accurate in the broader context of advisor–advisee:
    - It is not a *per se* fiduciary relationship
    - However, where 'the elements of trust and confidence and reliance on skill and knowledge and advice are present, the relationship is fiduciary and the obligations that attach are fiduciary'
    - Reliance may be total or partial
    - 'The relationship of broker and client is elevated to a fiduciary level when the client reposes trust and confidence in the broker and relies on the broker's advice in making business decisions.'
    - The broker must then 'do so fully, honestly and in good faith.'
  - This is 'an accurate statement of fiduciary law in the context of independent professional advisory relationships, whether the advisers be accountants, stockbrokers, bankers or investment counsellors. Moreover, it states a principled and workable doctrinal approach.'
  - There are important policy reasons why financial advisers should owe fiduciary duties to their clients:
    - 'These are occupations where advisors to whom a person gives trust has [sic] power over a vast sum of money, yet the nature of their position is such that specific regulation might frustrate the very function they have to perform. By enforcing a duty of honesty and good faith, the courts are able to regulate an activity that is of great value to commerce and society generally.'
    - 'Professor Weinrib speaks in terms of "maintaining the integrity of the marketplace".'

- The existence of professional codes also supports this conclusion
  - ‘The *raison d’etre* of such codes is the protection of parties in situations where they cannot, despite their best efforts, protect themselves, because of the nature of the relationship. These codes exist to impose regulation on activity that cannot be left entirely open to free market forces.’
  - ‘[T]he rules set by the relevant professional body are of guiding importance in determining the nature of the duties flowing from a particular professional relationship.’
  - With respect to the accounting profession, the relevant rules and standards evinced a clear instruction that all real and apparent conflicts of interest be fully disclosed to clients, particularly in the area of tax-related investment advice. The basis of this requirement is the maintenance of the independence and honesty which is the linchpin of the profession’s credibility with the public.’

- Unless there is fully informed consent to the conflict of interest, there will be a breach of fiduciary duty
  - ‘The essence of professional advice is trust and confidence, and a professional adviser must act in their client’s best interest to the exclusion of all other interests, unless there is disclosure [of those other interests]’

- There must, however, be actual and reasonable reliance on the adviser
  - Essentially, ‘equity does not help the fool’
  - Industry practice will also be relevant to this assessment (eg, if it is normal to protect confidential information with non-disclosure agreements, and a vulnerable party does not utilise such a protective measure, equity may not come to their aid)
  - Normally, advisees are entitled to accept and trust the advice of their financial advisers
  - ‘In the advisory context, the advisor’s ability to cause harm and the client’s susceptibility to be harmed arise from the simple but unassailable fact that the advice given by an independent advisor is not likely to be viewed with suspicion; rather, it is likely to be followed’
  - This requirement is less explicit in the Australian case law

- Application:
  - ‘It lies ill in the mouth of the respondent to argue that the appellant was not vulnerable to a breach of loyalty when he himself concedes that loyalty was the central feature of the parties’ business relationship. As it turned out, of course, the respondent used the position of ascendency granted him by the appellant to line his own pockets and the pockets of his developer clients.’
  - The parties were in frequent telephone and personal contact
  - Mr Hodgkinson was identified as one of Mr Simms’ ‘special’ clients
  - There was no referral to independent third parties for investment advice
  - Trial judge: ‘In effect, Mr Simms assumed the responsibility for Mr Hodgkinson’s choice. He analysed the investments, he recommended the investments, and he effectively chose the investments for Mr Hodgkinson’
  - As a result, Mr Hodgkinson ‘approached the meeting with “chequebook in hand”’

        - Even though Mr Hodgkinson made other investments with other advisers, this does not mean that he did anything but rely on Mr Simms for the particular investments being considered
        - Mr Simms breached his duty to Mr Hodgkinson by not disclosing his pecuniary interest with the developers

    - Remedy:
        - The proper approach to damages is restitutionary: Mr Hodgkinson is entitled to be put in as good a position as he would have been in had the breach not occurred'
        - This means restoring Mr Hodgkinson to his position before investing in the units
        - Trial judge: return of all invested capital, including consequential losses, minus the amount Mr Hodgkinson saved on income tax due to the investments
        - On appeal, Mr Simms argues that Mr Hodgkinson would still have invested in the tax shelters even had he known the true facts
            - This is not supported by the facts
            - The non-disclosure was material, so the counter-factual scenario cannot be assessed without separate evidence
            - In general, 'where the plaintiff has made out a case of non-disclosure and the loss occasioned thereby is established, the onus is on the defendant to prove that the innocent victim would have suffered the same loss regardless of the breach: *London Loan & Savings Co v Brickenden*'
        - Mr Simms also argued that, since it was the real estate market which directly caused the investments to lose their value, non-disclosure was not the 'proximate cause' of Mr Hodgkinson's loss
            - Instead, he argues, the loss was caused by the general economic recession that hit the British Columbian real estate market in the early 1980s, so that it would be 'grossly unjust' to hold Mr Simms accountable
            - However, Mr Hodgkinson would not have invested in the units but for Mr Simms' material non-disclosure
            - Therefore, the fact remains that Mr Hodgkinson 'would not have been exposed to *any* of the risks associated with these investments had it not been for [Mr Simms'] desire to secure an improper personal gain. In short, … it was the particular fiduciary breach that initiated the chain of events leading to the investor's loss. As such it is right and just that the breaching party account for this loss in full.'
            - Policy argument:
                - 'Like-minded fiduciaries in the position of [Mr Simms] would not be deterred from abusing their power by a remedy that simply requires them, if discovered, to disgorge their secret profit, with the beneficiary bearing all the market risk. If anything, this would encourage people in his position to in effect gamble with other people's money, knowing that it they are discovered they will be no worse off than when they started. As a result, the social benefits of fiduciary relationships, particularly in the field of independent professional advisors, would be greatly diminished.'
            - Mr Hodgkinson is entitled to be retained to the pre-transaction

status quo

- Sopinka and McLachlin JJ (dissenting):
  - Factual disagreement: there is insufficient trust and confidence in the relationship
    - Mr Hodgkinson looked to Mr Simms for advice and accepted it
    - However, he did not do so unreflectively, instead discussing each investment with Mr Simms, receiving an accurate written description of each development, and estimated financial projections and tax savings
    - Finally, Mr Hodgkinson chose to invest
    - In these circumstances, 'the plaintiff was not peculiarly invulnerable, let alone at the mercy of or under the domination of the defendant'
  - Legal disagreement:
    - There must have been a 'seeding' and acceptance of the power, which there was not here
    - Vulnerability encompasses all three characteristics of fiduciary relationships identified in *Frame*: it 'connotes a relationship of dependency, an "implicit dependency"'
    - Vulnerability is crucial, and not sufficiently present here
    - The 'imposition of fiduciary obligations in some cases may be justified on the ground of "maintenance of the public' acceptance of, and the credibility of, important institutions in society which render 'fiduciary services'". But neither of these rationales would appear to justify imposing a fiduciary obligation on the purveyor of investment advice where the client retains the power and ability to make the decisions of which he later complains.'
  - Importantly, however, the minority do not dismiss the possibility that financial advisers can owe fiduciary duties in some situations:
    - 'We add that this does not mean that advisors, financial or otherwise, can never be subject to fiduciary obligations. Each relationship must be examined on its own facts. A relationship where one party unreflectively and automatically accepts the advice of the other might raise different considerations. The critical question, as noted earlier, is whether there is total assumption of power by the fiduciary, coupled with total reliance by the beneficiary. In short, that the beneficiary was vulnerable in the sense of being at the mercy of the fiduciary's discretion.'
    - 'That is not, on the evidence, the sort of relationship which is before us on this appeal … [so] no fiduciary obligation arises.'

<u>Decision</u> (majority)

- Here, the plaintiff was vulnerable, and reposed trust and confidence in the defendant
- There is a relationship of power–dependency between the parties
- Here, there was no disclosure of the conflict, so the duty was breached
- Here, the plaintiff did rely — reasonably — on the defendant's advice

Chase Manhattan Bank v Israel–British Bank is a puzzling anomaly of a case. It appears to stand for the proposition that a fiduciary relationship can arise without any undertaking, nor indeed any trust or confidence. Fiduciary obligations are said to arise the instant money is paid into the wrong hands, the content of those obligations being to return the misplaced funds. Vulnerability appears to underlie this approach, though when dealing with two multinational banks such an analysis hardly seems convincing. In light of established principles, and with great respect to the Court, this case appears more as a rationalisation of a remedy than a considered decision predicated upon the existence of actual fiduciary obligations.

***Chase Manhattan Bank v Israel–British Bank* (1981) UK Ch:**

Facts
- The plaintiff, Chase Manhattan Bank, transfers £2m into the defendant's bank account
- Later that day, a second transfer of £2m is made as a result of a clerical error
- The defendant becomes insolvent and is put into receivership
- Consequently, the plaintiff could only fully recover its money if it obtained a constructive trust over the wrongly transferred money
- If the plaintiff received a personal remedy, it would be an unsecured creditor and fail to receive the full amount; this is because the £2m would form part of the defendant's assets to be distributed according to insolvency law
- Proprietary remedy: £2m would be returned to the plaintiff as secured creditor
- This is really a contest between the plaintiff and the defendant's unsecured creditors

Issue
- Was there a breach of fiduciary duty?

Reasoning
- The fiduciary relationship arose by virtue of the mere fact that there was payment into the wrong hands
    - Where is the undertaking of the defendant to act in the interests of the plaintiff?
        - There is arguably vulnerability, but not trust and confidence and certainly not reasonable reliance (the plaintiff was a bank, after all)
        - Is the Court reasoning backwards from a desire to grant a remedy?
    - Perhaps this just adds ammunition to the argument that courts distort concepts of fiduciary duties in order to impose a constructive trust where morally required
        - Ie, an *ex post facto* rationalisation
    - Other argue on the basis of restitutionary principles (enrichment, unconscionable to retain) that this should be sufficient to give rise to a proprietary remedy of constructive trust
    - Here, however, the Court adopts a traditional argument but fails to explain the result; arguably distorts the concept of fiduciary indicia

Decision
- A fiduciary relationship existed and was breached by failing to return the funds

D *Models of Fiduciary Obligation*

Broadly speaking, there are two approaches to determining whether fiduciary obligations exist and, if they do, their scope and content: the proscriptive and prescriptive models.

The proscriptive approach emphasises the negative obligations of a fiduciary (that is, behaviour that is proscribed or prohibited by equity). For example, a fiduciary, it is said, must *not* create a situation of conflict between their interests and those of the principal. They *cannot* reap a profit from the relationship without their principal's consent. This approach dominates the Australian case law.

By contrast, the prescriptive approach emphasises the positive obligations of a fiduciary — circumstances in which the fiduciary will be obliged to act. For example, the fiduciary *must act* in the best interests of the principal, and *must make* full disclosure of anything relevant to the relationship. Canadian case law is characterised by this approach.

Issue: should fiduciary obligations be construed more broadly? That is, should fiduciary remedies be more widely available, and is the Australian proscriptive approach too narrow? Is it appropriate for equity to solely protect narrow pecuniary interests, or would it be better to adopt a broader Canadian-style approach encompassing prescriptive duties? Can the dichotomy between these paradigms of fiduciary duty be sustained?

These models are now examined and critiqued in turn.

1 *Proscriptive*

The Australian approach emphasises pecuniary interests. Conflict must be financial. Interests are economic, relationships commercial. By contrast, Canadian courts have recognised non-financial interests, such as bodily integrity, emotional harm and other personal interests. As a result, Canada recognises more personal relationships, and more obligations within those relationships — such as a doctor's duty to disclose information to their patients — as fiduciary.

Another characteristic of the proscriptive approach is that it tends to invert the enquiry, first asking: 'Is there any subject matter to which a fiduciary duty could attach?' (Has a party made a financial profit? Is there a recognised conflict of interest?) If no relevant subject matter exists, the enquiry ends. If there is a profit or conflict in the narrow financial sense, then the enquiry may proceed to examine whether such an obligation is owed. ('Is the relationship of a fiduciary character?') Thus, instead of commencing by an examination of the *character* of the relationship, the Court first examines the duty that is alleged to have been breached (see *Breen v Williams*). It examines the conduct of the parties, *then* considers their relationship.

Breen v Williams (1996) HCA:

Facts

- Dow Corning manufactures a silicone breast implant; due to a design defect, it leaks and causes harm to those in whom the devices were implanted
- Julie Breen has had an implantation surgery, and the implants subsequently leak
- She undergoes corrective surgery, but it fails to relieve her pain and resolve the problem
- She wants to join in a class action lawsuit against the United States manufacturer
- Permission to do so is granted, providing that she submits medical records to the American Court documenting her treatment and injuries
- To obtain these records, Ms Breen must access them from her Australian doctor
- However, her doctor, a Mr Williams, refuses to grant access to the files (though he agreed to provide a report summarising the information), unless she indemnifies him against all liability for performing the corrective augmentation surgery
- She sues Mr Williams in contract, property and breach of fiduciary duty
    - She claims a contractual right to her medical records; that is, that Mr Williams owed a contractual duty to disclose
    - She claims that the records were her property, not those of her doctor of the health service
    - In equity, she argues that the doctor owes her a positive fiduciary duty to disclose to her details of her medical records (relying on *McInerney v McDonald*)
- Strangely, Ms Breen does not simply sue Mr Williams in negligence and thereby obtain discovery of the records
    - If the litigation takes place in a foreign jurisdiction, letters rogatory will normally be issued from the foreign judge requesting access to the documents
    - Instead, Ms Breen pursues a test case, intending to establish whether a medical

patient can obtain access to their records at common law

Issue
- Does Mr Williams owe a fiduciary obligation to Ms Breen to make full disclosure of her medical records?

Reasoning
- Court of Appeal of the New South Wales Supreme Court:
  - Mahoney JA:
    - Courts should not legislate, just apply the law; the fiduciary relationships should not be judicially expanded when it is Parliament's responsibility to enact medical records legislation
    - Refers to *McInerney v MacDonald* with disapproval; prefers the English position (no access to medical records by virtue of fiduciary obligation)
    - Therefore, there is no fiduciary relationship between a doctor and their patient
    - Consequently, Ms Breen has no right of access to her records

  - Meagher JA:
    - Ms Breen could have subpoenaed the records from Mr Williams — there was another means by which she could have obtained the records; instead, she chose to pursue a theoretical test case
    - No general doctor–patient fiduciary obligations exist
    - The Canadian cases have widened the scope of fiduciary relationships to the point where the concept is devoid of all meaning
    - Doctors may owe limited fiduciary duties to their patient, but this is restricted to:
      - Not making unauthorised profit; and
      - Not revealing confidential information
      - (Both proscriptive duties)
      - [What about conflicts of interest? See, eg, Gummow J]
    - Profit disgorgement is the essence of fiduciary law: a materialistic mechanism to return money from those unjustly enriched by their relationship with the plaintiff

  - Kirby JA (dissenting):
    - No common law right of access exists as a matter of tort or contract
    - However, there is a right of access by virtue of fiduciary law
    - *Freedom of Information* legislation already allows patients to access their public hospital records; suggests that society supports access to private documents as well
    - The fact that she could have obtained a subpoena to gain access *also* supports (rather than detracts from) her argument to obtain access through fiduciary law — demonstrates that access is consistent with established doctrine and community values (note opposite reasoning from same facts to Meagher JA)
    - In the Canadian and United States jurisdictions, there is a culture of giving access to patients — informing patients, consultative, relationship of equality (cf England: 'doctor knows best', private notes)
    - Strong policy arguments for greater disclosure between doctors and patients (despite issues in some cases regarding detrimental information, risk of self-harm, etc)
    - Note tension between autonomy and paternalism (over-regulating professions, forcing fiduciaries to act in best interests, etc: yet,

advocates of doctor–patient fiduciary relationships argue that they should be less paternalistic! Perhaps, according to Kirby JA, the fiduciary relationship *encourages* equality)

        - Doctrinal issues:
            - Fiduciary relationships are created by judges pursuant to doctrines of equity
            - Consequently, judges should be responsible for developing their scope and content over time
            - A fiduciary's core obligation is to act in the principal's interests when he or she is especially vulnerable to harm
            - These duties protect fundamental personal, as well as financial, interests

- High Court of Australia:
    - Brennan CJ:
        - Fiduciary duties have two sources:
            - (1) Agency (undertaking to act for another)
            - (2) Ascendancy, influence, dependency or trust (vulnerability)
        - First, identify the subject matter to which the fiduciary obligation relates (conflict, profit, etc)
        - It is wrong to treat the fiduciary obligations as extending to all aspects of the fiduciary's conduct in the relationship
        - The scope of the duty must be shaped according to the factual circumstances
        - In the context of a doctor–patient relationship:
            - There is no agency or undertaking to act in the patient's interests
            - However, there are vulnerability elements
            - Thus, there are some fiduciary elements, but not others
            - The consequence is that a doctor must bear the onus to establish that any gifts they receive from their patient were procured free from influence
        - Canadian case law on fiduciaries does not represent the law of Australia
        - Here, no relevant subject matter over which a doctor's fiduciary duty is extended (ie, access to medical records doesn't involve property wrongly taken, profit wrongly made or conflict wrongly entertained)

    - Dawson and Toohey JJ:
        - A doctor's duty is ordinarily in contract and tort (reasonable care and skill in giving treatment and advice)
        - These duties are narrow and do not encompass the entirety of the relationship (duty of confidentiality, presumption of undue influence for gifts)
        - Fiduciaries act in a representative character, but doctors do not (no undertaking to act in the interests of a patient)
            - The doctor is simply obliged to exercise professional responsibility
            - By contrast, fiduciary duties involve conflict and profit
            - These concepts are inappropriate to ascribe to a doctor treating a patient
            - Unlike a lawyer–client relationship (clearly fiduciary)?
                - Negligent advice may also amount to breach of fiduciary duty
                - However, advice might be negligent without breaching a

fiduciary duty
        - Eg, advising a client negligently without any conflict or profit
        - Eg, advising two clients to same transactions: conflict, though advice may be correct
        - Lawyer–client relationship has a representative aspect: appearances, primary decision-making
        - Cf doctor–patient: doctor rarely if ever makes a decision about a procedure or medicine without the patient’s consent
    - Court treats doctor–patient as professional, arms-length relationship
        - Arguably inaccurate
        - Contradicts earlier paternalism argument: if parties are truly independent, access to records should be justifiable on the basis of being a professional customer
        - It is also arguably a more intimate relationship than lawyer–client (medical patients are vulnerable, and must be protected against invasive procedures and disclosure of private or personal matters: Canadian approach)
        - [Or perhaps the court is simply assuming that, as a privileged relationship, doctors would never engage in wrongful conduct, so that they will only be fiduciaries to the extent that they could actually do so in the circumstances — this seems unconvincing]
    - A fiduciary duty could be superimposed on contractual or tortious obligation (eg, where the doctor owns the pathology laboratory and recommends tests, or where the doctor receives a gift or there is a conflict between patients), but normally the obligations in contract and tort will be sufficient to cover the field
    - The Canadian authority should not be followed: ‘We do not view a doctor’s relationship with a patient in Australia as requiring utmost good faith and loyalty’
        - Arguably, this is at odds with community perceptions
    - Policy considerations should not have a role to play in expanding equitable doctrines

- Gaudron and Deane JJ:
    - The relationship between a doctor and his patient is characterised by inequality of bargaining power: the doctor has power and knowledge, upon which and upon whom the patient is dependent for advice, and without whom is vulnerable
    - A doctor–patient relationship does bear some of the characteristics traditionally associated with fiduciary relationships
    - In some cases, dependence by the patient may give rise to a fiduciary duty
    - However, in general, the relationship is not fiduciary
    - The relationship, if it exists, would cover diagnosis, advice and treatment (but not the whole relationship)
    - However, there is no fiduciary duty concerning access to medical records (no conflict of interest, no unauthorised profit)
    - Thus, the existence of the relationship depends on the potential for breach of duty
        - This relates to the inversion point

- Gummow J:

- The fiduciary principle monitors the abuse of a loyalty reposed
    - 'The relationship between medical practitioner and patient who seeks skilled and confidential advice and treatment is a fiduciary one. That will be so regardless of whether it is because the relationship between the parties is one which gives the medical practitioner a special opportunity to affect the interests of the patient who is vulnerable to abuse by the fiduciary of his position, or because the medical practitioner undertakes to exercise professional skill for the benefit of the patient, and particular reliance is placed upon the medical practitioner by the patient.'
    - 'In a real sense, especially if invasive procedures upon the person of the patient are involved, the patient has delegated control to the person providing health care. Further, for the patient to obtain the benefit sought from the relationship the patient often must reveal confidential and intimate information of a personal nature to the medical practitioner.'
    - 'Finally, the efforts of the medical practitioner may have a significant impact no merely on the economic but upon the fundamental personal interests of the patient.'
    - These considerations illustrate why the relationship has 'a fiduciary element'

- Thus, because there is a 'special opportunity' to affect the interests of a vulnerable patient, the doctor–patient relationship *can be* fiduciary:
    - Unlike the other justices, Gummow J accepts that there is an undertaking to act in the best interests of the patient
    - However, the extent of the fiduciary obligations must be considered in particular cases to determine 'the subject matter over which the fiduciary obligations extend'
    - The extent of the obligation concerns medical treatment and ensuring there is no conflict of interest
        - [Is this just medical treatment, or would it extend more broadly to advice or consultation?]

- However, disclosure of medical records does not fall within the scope of these fiduciary duties, since there is no possibility of conflict or misuse of the fiduciary position
    - The situation might be different if the facts were characterised as the doctor not wanting to give the records because he doesn't want to be sued (clear conflict of interest)
    - In such a case, there would be a direct conflict between giving the damaging records and protecting own interests — the fiduciary doctor would be unable to discharge adequately the one obligation without conflicting with the observance of their own personal interest in avoiding payment of compensation, legal expenses and in maintaining their reputation
    - The Court appears to reject this argument; this suggests that the concept of conflict is very narrow: pecuniary only (even though threat of litigation is arguably a pecuniary loss)
    - Seeking access to medical records falls outside the scope of treatment or conflict

- However, there are circumstances in which genuine issues of conflict

and unauthorised profit may arise; Gummow J poses several examples:
- Where the doctor recommends one of a number of equally suitable pharmaceutical drugs solely on the basis that the doctor receives a payment or commission for such a prescription, or other 'side-benefits from the manufacturer'
- Where the doctor recommends a patient undergo treatment at a particular private hospital where the only reason for the recommendation is that the doctor has a financial interest in the hospital
- These examples would be clear breaches of fiduciary duty

▪ Approves the Californian case of *Moore v Regents of the University of California* (1991):
  - Doctors remove the patient's spleen, not for medical reasons, but because they wanted to use it to develop a 'cell line' over which they were able to take out a patent for medical technology
  - That is, the doctor used the body parts to make a profit
  - This constituted a breach of fiduciary duty (body parts are not objects of property, but a doctor who uses them for financial profit is still in breach)
  - Fully informed consent would have been a defence (eg, if the doctor had told the patient of his interest and their intended use for the spleen
  - However, must have been fully informed of the nature of the transaction
  - Informed consent is, in general, always a defence to breach of fiduciary duty
  - The remedy in *Moore* is for the doctor to hold the patent, when granted, on constructive trust for the patient
  - The patient therefore holds all rights arising from the patent, including an entitlement to any royalties derived from exploitation of the invention
  - Gummow J: this is good law in Australia

▪ In essence, the relationship will only be fiduciary to the extent that the practitioner can entertain unauthorised conflict or profit
  - 'the fiduciary principle would monitor the abuse of loyalty reposed in the medical practitioner by the plaintiff'
  - 'The abuse of duty would involve derivation of a benefit or gain by use or by reason of the fiduciary position of an opportunity or knowledge which resulted from it'
  - Just because a doctor may also be a trustee, this does not mean that they owe a quasi-tortious duty to act solely in the best interests of their principals; 'informed consent' may operate to relax this somewhat

▪ The duty alleged in the present case goes beyond the scope of these fiduciary restraints on improper conduct:
  - 'The present is not a case where, unless the respondent accedes to the right asserted against him by the appellant in this proceeding, the respondent will have derived a gain or benefit at the expense of the patient, beyond the agreed fee.'
  - 'Nor will Dr Williams have put himself in a position where his interests conflict [or could possibly conflict] with those of [his]

patient.'
- '…to show that a medical practitioner owes fiduciary duties in certain circumstances to the patient is not to demonstrate a right in the patient to inspect and to take copies of the notes and records of the medical practitioner'
- The fact that, as was said in *McInerney v MacDonald*, access to records is needed to determine whether the practitioner had fulfilled their fiduciary duties with utmost good faith and loyalty (and hence 'to promote the proper functioning of the relationship'), does not mean that a duty to disclose such records will be fiduciary
- Here, Breen does not seek the documents (she could, after all, have received a report summarising that information) but, rather, an extra-curial right to obtain discovery of them without engaging with the proper processes of the Court (she could have sued Williams and hence proceeded with discovery in the normal course of things)
- Further, Breen does not allege any impropriety on the part of the doctor — there is no issue of unauthorised conflict or profit
- The interests of Breen are to be protected by the general law (both of negligence and contract, and civil procedure more generally)

- Essentially, a court will only grant a remedy in respect of a fiduciary obligation if
  - In the case of a negative obligation, the practitioner has breached it (remedy) or is going to breach it (injunction)
  - In the case of a positive obligation, the same (however, no positive obligations exist)
- Broadly, doctors' fiduciary duties extend only to not profiting from their position and not conflicting with their patients' interests
- Here, a different, *positive* obligation is alleged to have been breached
- This obligation is not fiduciary since it does not fall within the scope and ambit of the recognised *negative* fiduciary duties
- Consequently, no remedy is available

<u>Decision</u>
- Majority: there is no general fiduciary relationship in existence between doctor and patient
  - There is no broad fiduciary relationship between a doctor and a patient so as to create a duty to disclose patient records (unanimous)
  - On certain facts, it may be possible to allege a proscriptive duty in relation to the traditional obligations of fiduciaries
  - However, there is not here any such relationship, and any posited breach falls outside the scope of cognisable duties
  - Thus, the doctor–patient relationship can be fiduciary where there is such a conflict or profit
- Gummow J:
  - The doctor–patient relationship is fiduciary only to the extent that it would be a breach of duty for the doctor to make unauthorised profit or to create a possibility of conflict between the doctor and his patient
  - However, if the alleged duty goes beyond profit or conflict — such as to some positive duty of disclosure — then it will fall to be governed by the general law and not by equitable fiduciary law

Breen v Williams is authority for the proposition that the proscriptive model governs the content and scope of fiduciary obligations in Australia. It is sometimes accorded the further authority of stating that Australian fiduciary law protects economic interests against narrow categories of breach, being unauthorised profit or a real possibility of conflict.

The majority in *Breen v Williams* held that the relationship of medical practitioner and patient does not, without more, create fiduciary obligations. Justice Gummow concluded that such a relationship was indeed fiduciary because of the doctor's undertaking to treat and the patient's vulnerability. However, the fact that the relationship has fiduciary elements is only one aspect of determining a claim for breach; a second stage relating to the facts of the case must be applied. This second stage considers the scope of the fiduciary duties; in particular, whether the conduct alleged to amount to breach falls within their scope. On the facts, Gummow J appears to have held, in effect, that the so-called 'duty' to disclose was not within the scope of the duty to advise, and for this reason was not fiduciary. This meant that failure to disclose was not in breach.

Despite these relatively narrow conclusions as to fiduciary duties, *Breen v Williams* is commonly misconstrued as standing for the general proposition that fiduciary duties are restricted to economic interests. However, no judgment ever explicitly states that fiduciary interests are owed only in respect of financial interests. The most that can be said is that, on the facts of the case, the duty of disclosure is not capable of being given fiduciary content.

Nevertheless, subsequent cases have taken heed of *Breen v Williams*' restrictive approach. *Breen v Williams* has significantly influenced the further development of fiduciary principles in Australia. It has signalled a halt to the expansion of fiduciary relationships. Judges are now especially reluctant to treat parents as owing fiduciary duties to their children: see, eg, *Paramasivam v Flynn*.

Subsequent to the decision in *Breen v Williams*, the New South Wales government passed legislation granting patients access to medical records held by their private practitioners.

Pilmer v Duke Group Ltd (in liq) ('*Pilmer v Duke*') further narrows the proscriptive model. This is a case which concerns economic interests. The High Court of Australia held that there must be both a real and sensible possibility for conflict of interest before there can be breach of fiduciary duty. If this level of conflict does not exist, and there is no unauthorised profit, then no fiduciary duties can arise at all.

Pilmer v Duke Group Ltd (in liq) **(2001) HCA:**

Facts

- Kia Ora Gold Corp NL ('Kia Ora') seeks to takeover Western United Ltd
- In order to initiate the takeover, ASX *Listing Rule* 3J(3) requires that an report be furnished upon shareholders to the effect that the amount being offered is a 'fair price'
- That report is supposed to be supplied by an independent, qualified person
- Kia Ora offers $26 178 135.81 in cash and the issue of 68 000 000 shares
- The accountant, a Nelson Wheeler, belongs to a firm comprising Pilmer and others; he says that this is a fair price
- In fact, $26m is an outrageously excessive valuation of the company, which in reality is worth about $6 439 339
- There is some suggestion that Wheeler does not want to say 'no' to the acquisition, since he knows that his firm will receive further work for Kia Ora if all is successful
- Kia Ora takes over Western United, then subsequently becomes insolvent as a result of

having paid so much money
- It changes its name to Duke Group Ltd ('Duke Group')
- During the winding up, the liquidator of Duke Group sues the accountants (Pilmer and partners), alleging:
  - That the report was negligently prepared
  - That there was a breach of contract
  - That Pilmer breached fiduciary obligations it owed to Kia Ora
- Trial judge: Pilmer was negligent and breached their contract, but there was no breach of fiduciary duty by them
- Full Court of the Supreme Court of South Australia: there was a breach of fiduciary duty

<u>Issue</u>
- Did a fiduciary relationship exist between Kia Ora and Pilmer?
- If so, did the giving of Pilmer's report in the circumstances in which it did so amount to a breach of duty?

<u>Reasoning</u>
- McHugh, Gummow, Hayne and Callinan JJ:
  - There are two alleged conflicts:
    - Nelson had hoped to continue advising if the merger went ahead successfully (financial interest in the possibility of future audit work)
      - There is not a 'real and sensible possibility' that this would ever create a conflict of interest because the conflict is not sufficiently serious
      - There is a theoretical conflict perhaps, but it is not serious enough to warrant breach of fiduciary duty
      - Besides, auditors will *always* hope for future work — indeed, many will expect it because follow up work upon completion of a successful task is a standard commercial practice
    - The directors of Pilmer had sold personal shares in Western United for a lower price than that being paid in the takeover, but did not tell Kia Ora this because the accountants had personal friendships with its directors
      - This is relevant to negligence but not fiduciary duties
      - A narrow view of conflict is adopted — there is no financial conflict of interest here
  - There can be overlap between tort and fiduciary law
  - In some circumstances, a financial adviser may owe fiduciary duties to a client
    - As a preliminary matter, here, the accountants did not give financial advice to the client (did not advise whether to proceed with the takeover)
    - All they did was provide an opinion about pricing for the purposes of the report [but is this still advice?]
  - Cite *Breen v Williams* with approval: Australia follows a proscriptive (rather than prescriptive) approach: duties not to profit or create a conflict
  - Here, in the absence of ascendency, influence, dependence upon or trust of the accountants, it cannot be said that there was a fiduciary duty
  - The allegation of Kia Ora that there was some prior or concurrent engagement or undertaking by Pilmer that created a real or substantial possibility of conflict is only expressed in a general way — that they expected that 'mutual dealings' might continue if they answered Kia Ora's proposal favourably
    - This falls short of demonstrating that there is a 'real or substantial possibility of conflict [as] spoken of in the authorities': at [82]
    - 'Conflict is not shown by simply pointing to the fact that there had been past dealings between the appellants and interests associated with the Kia Ora directors.'

        - 'Nor is it sufficient to say generally that there was a hope or expectation of future dealings. That will often be so. Most professional advisers would hope that the proper performance of the task at hand will lead the client to retain them again. No real or substantial possibility of conflict was demonstrated.'
    - *Remedial issue*: can contributory negligence affect the relief obtained for brief of fiduciary duty?
        - There is conceptual difficulty involved in accepting contributory negligence in a fiduciary claim: [86]
        - Contributory negligence focuses on the plaintiff's conduct
        - However, fiduciary law is concerned with the defendant's conduct
        - 'It follows that the allowance by the Full Court of the sum for the issue and allotment of Kia Ora shares, in assessing the damages for breach of contract or negligence, is not to be sustained on the footing that there was a fiduciary duty owed by the appellants, breach of which brought with it a measure of equitable compensation in the same sum'

- Kirby J (dissenting):
    - 'This appeal, in my opinion, is mainly concerned with fiduciary obligations. It involves the ambit of a propounded fiduciary duty, the remedies available where such a duty is found to have been breached, and, specifically, whether such remedies may be modified by a conclusion that there has been "contributory fault" on the part of a beneficiary.'
    - On the facts:
        - There is 'financial advice'
        - There is a fiduciary relationship
        - There is a conflict of interest, and hence breach of fiduciary duty
    - Acknowledges that he is bound to follow *Breen v Williams* majority
        - 'While I respectfully adhere to the opinions which I expressed in *Breen v Williams*, I must be careful, in applying the law to the present appeal, to conform to the ratio of *Breen* in this [C]ourt, including as it appears in any reasoning which, by inference, is incompatible with what I said in the Court of Appeal.'
        - However, notes that there were different rationales for the *Breen* decision
            - The 'majority' found no fiduciary relationship, but Gummow J found that the relationship in respect of medical treatment and advice is fiduciary
            - There is no presumptive category of fiduciary relationship existing between advisers and their clients
        - *Breen* does not completely reject Canadian authority
        - *Breen* does, however, entail the adoption of a proscriptive approach in Australia (though Kirby J does question the utility of the dichotomy)
    - Kirby J discusses the ratio of *Breen* in some detail; it is useful to set this discussion out in full
        - '**[119]** When one examines what *Breen* actually stands for, as a matter of legal authority, it clearly negates any entitlement by patients, under the common law, to inspect their medical records, save with the agreement of the medical practitioner concerned or where legislation so provides.'
        - '**[120]** … A majority were clearly of the opinion that the relationship of medical practitioner and patient did not, without more, create fiduciary obligations. Thus, that relationship bore no sufficient analogy to that between a solicitor and client, or trustee and *cestui que trust*, that traditionally gives rise, without more, to fiduciary obligations.'

- ‘On the other hand, Gummow J concluded that the relationship between a medical practitioner and a patient who seeks skilled and confidential advice and treatment was indeed a fiduciary one.’
- ‘**[121]** In some established relationships, the relationship itself will be enough to make it clear that a fiduciary obligation is owed by one party to the other in respect of related transactions between them during the relationship. Relationships giving rise to such obligations differ between jurisdictions. In Australia, Gaudron and McHugh JJ in *Breen* mentioned “trustee and beneficiary, agent and principal, solicitor and client, employee and employer, director and company and partners”. However, in other countries, perhaps reflecting different social circumstances, courts have been willing to add new and different categories. Thus in Canada, the Supreme Court has added (but this [C]ourt has not) the category of medical practitioner and patient. That [C]ourt has also added the relationships of parent and child and the Crown and indigenous peoples. In the United States of America still further relationships have been added. These include majority and minority shareholders, patients and physicians, or psychiatrists and others.’
- ‘**[122]** The primary point for which *Breen* stands in relation to fiduciary duties is that, in Australia, attempts to elevate a relationship between medical practitioner and patient effectively to a special one which, without more, will import fiduciary obligations has [sic], for the moment, failed. Proving that the relationship involves an imbalance of power, and even vulnerability on the part of the patient, was not sufficient.’
- ‘**[125]** … I do not read *Breen* as obliging Australian courts to ignore all Canadian and United States authority on fiduciary obligations. There remains much in the law of those jurisdictions which is common to Australian law so far as equitable doctrine and remedies are concerned. The basis for fiduciary duties in all jurisdictions is explained in common terms by reference to obligations of loyalty to a person dependent on another who, to the knowledge of that other, is specially vulnerable.’
- ‘**[126]** Thirdly, *Breen* illustrates a general disinclination of Australian law to expand fiduciary obligations beyond what might be called proprietary interests into the more nebulous field of personal rights, such as those agitated in *Breen* itself. There the patient had no proprietary rights of any kind in the notes of the medical practitioner. The kinds of disputes concerning alleged fiduciary obligations that typically find their way to the courts usually involve financial relationships. Fiduciary obligations were never limited to disputes about property interests. Nevertheless, *Breen* stands as a warning that the imposition of fiduciary obligations “gives rise to proprietary remedies that affect the distribution of assets in bankruptcies and insolvencies”. This represents a further reason for exercising restraint in expanding the categories of *per se* relationships or treating new fact situations as attracting fiduciary obligations beyond those accepted in the past.’
- ‘**[127]** Fourthly, and most importantly, *Breen* upholds the principle stated in the aphorism that fiduciary obligations are “proscriptive” and not “prescriptive”. This, in my view, is the fundamental reason why all members of this [C]ourt in *Breen* rejected Ms Breen’s claim of a fiduciary obligation. Whatever the differing views which the justices held concerning the character of the relationship in question there and whether it was, or was not, a fiduciary one for some or all purposes, there was agreement that Ms Breen’s claim failed because it would have involved imposing on the suggested fiduciary positive obligations to act. It would have burdened him with an affirmative obligation to grant access

    - to his notes to a patient ("prescriptive" duties). It would thus have gone further than the conventional ("proscriptive") duties of loyalty, avoiding conflicts of interest or of misusing one's power, such as fiduciary duties have traditionally upheld.'
    - '**[128]** While, for my own pat, I question the viability of this supposed dichotomy (because omissions quite frequently shade into commissions) I must accept that *Breen* embraces the distinction. … Until further elucidated by this [C]ourt, it should therefore be followed by Australian courts and by me.'
  - However, *Breen* does not exclude the *very possibility* of a fiduciary obligation from arising between doctor and patient, and nothing said in *Breen* directly decides the present case
    - Kia Ora does not allege that the relationship of chartered accountant to client is *per se* fiduciary (ie, a presumed category)
    - Instead, it argues that such a relationship existed on the facts (ie, as a novel factual category of fiduciary relationship)
    - '…nothing in *Breen* speaks against the recognition of fiduciary obligations in the kind of relationship and activities proved by the evidence in this case. Indeed ,this was a classic case in which the proprietary interests of Kia Ora … were at stake.'
  - The argument being advanced is within the proscriptive approach: accountants deemed to be fiduciaries because of their relationship with the client must not profit without authorisation and must not entertain a conflict of interest
    - Here, proprietary rights are in issue; the impugned conduct concerns a negative duty (conflict of interest)
    - 'Although *Breen* was an invitation to enter new territory, this case is not. It is placed squarely in the middle of the kind of circumstance in which fiduciary obligations have been upheld on countless occasions: where the obligation of loyalty to the financial interests of identifiable persons who were specially vulnerable is abused by other persons entrusted with duties permitting them to make judgments, in effect, for others which called for the selfless pursuit of the interests of others, the independent performance of their duties and (if that be not possible) a refusal to be involved.'
    - This is not a case where prescriptive duties are alleged
      - Pilmer should have declined to provide the report pursuant to *Listing Rule* 3J(3)
      - This duty (to avoid conflict) was proscriptive, not prescriptive
  - The existence of fiduciary obligations in novel factual categories should be considered by reference to the following guidelines
    - '**[136]** … (1) Fiduciary obligations are not confined to established relationships or to exactly identical facts as those that have given rise to them in the past. Even those jurists most resistant to analogical extensions in this field accept that the list of persons owing fiduciary duties is not closed. It could scarcely be so, given that equity is itself the embodiment of judicial invention. Unless legislation requires a different approach, equity and equitable remedies respond to changing times, different social and economic relationships and altered community expectations.
    - '[I]t is essential that judges perform their functions by analogy from settled principles. They are not entitled to distort those principles. Nor may they superimpose an equitable classification on facts, simply because to do so would afford better or larger remedies to a plaintiff who appears to have suffered some wrong.'
    - '(2) Specifically, it is not sufficient, to impose fiduciary obligations on an

alleged wrongdoer, simply to point to the vulnerability of the person claiming to be wronged. … To turn every [disproportionate power relationship] into one giving rise to fiduciary obligations would be to distort basic doctrine.
… For fiduciary obligations, vulnerability to wrongdoing will certainly be a relevant consideration. However, it is not sufficient.'

- '(3) The mere fact that a party may have remedies at law, whether in contract or tort, does not exclude the possibility that fiduciary obligations may also be imposed. There is no antipathy between such concurrent obligations.'
- '(4) The greatest difficulty facing those who assert the existence of fiduciary obligations, outside the classic *per se* relationships, arises from the fact that the law has not formulated any precise or comprehensive definition of the criteria adopted for imposing such obligations.'
- '(5)' Vulnerability is too broad, confidence is too broad, acceptance of power for the benefit of another is simply a restatement of the problem rather than a useful criterion. However, professor's Finn's unifying principle is of some value: 'fiduciary obligations [arise] from the existence of a duty of loyalty that, reflecting "higher community standards or values", gives rise to a "legitimate expectation that the other party will act in the interests of the first party or at least in the joint interests of the parties and not solely self-interestedly". Essentially, this was the criterion that I favoured in *Breen v Williams*. While it can be criticised as tautologous and subjective, I still consider that it represents the best attempt to express what is involved.'
- '(6) … it is reasonable for courts to have regard to features commonly found in cases where fiduciary obligations have been upheld. Necessarily, such features are not exhaustive [and] may overlap.' They include:
  - The existence of a relation of confidence (*Breen* per Gaudron and McHugh JJ);
  - Inequality of bargaining power;
  - An undertaking by one party to perform a task or fulfil a duty in the interests of another party;
  - The scope for one party to unilaterally exercise a discretion or power which may affect the rights or interests of another;
  - A dependency or vulnerability on the part of one party that causes another party to rely on another; and
  - Loyalty (superimposed on all these instances).

- On the facts, there is a fiduciary duty obliging Pilmer not to act in a situation of conflict
  - Pilmer lacked independence
  - Pilmer's obligation to act solely in the interests of Kia Ora was 'compromised by and in substantial conflict with their personal and commercial loyalty to certain of the directors of Kia Ora'
  - This is evidenced by the fact that it failed to mention fundamental matters that should have been disclosed and disclosed to Kia Ora
  - The shareholders in Kia Ora relied on Pilmer, as did the larger community of potential investors in Kia Ora
  - Chartered accountants who accept the reporting function envisaged by rule 3J owe a duty of selfless loyalty to the client which commissions the report; here, this meant 'loyalty and integrity with respect to Kia Ora, the company, as distinct from its committed directors who were able to send a lot of business, as they had in the past, in he direction of the

appellants' firm'
        - The existence of this 'duty of loyalty and integrity', owed by the very nature of the task entrusted to Pilmer, means that it owed Kia Ora fiduciary duties when creating the report
    - Pilmer breached that duty of undivided loyalty
        - This breach could not have been repaired by disclosure, since it was a conflict relating to the very relationship they continued to have with Kia Ora's directors
        - Consequently, Pilmer should have declined to act at all
        - '**[144]** With all respect to those of a different view, this [C]ourt should not, by its decision in this case, send a signal that chartered accountants in the position of the appellants were merely the contracted agents of their client or simply a tortfeasor liable under the law of negligence'
        - '**[145]**' Pilmer argued that because Kia Ora knew of their past associations (ie, the facts giving rise to the conflict), but did not object, that they consented to the conflict
            - 'I disagree. This was not a case of informed consent. Such consent requires full and frank disclosure to the party affected of all material facts. It obliges the fiduciary to reveal to the beneficiary all relevant information necessary for the beneficiary to make a proper judgment as to whether to give consent to the activity that would otherwise be a breach of fiduciary obligations. No such disclosure was made here. … Indeed, there was no disclosure to the shareholders at all.'
        - [Kirby J seems to be construing conflict and profit by reference to broader facts than the majority]
            - His Honour adopts a conservative doctrinal approach but points more creatively to additional factors relevant to these criteria (despite being constrained by authority)
            - It is unclear whether, in a novel case before the High Court, a broader construction of the facts will be adopted, such as to make out a breach of fiduciary obligation
    - Equitable remedies serve to compensate and deter; here, clear loss to Kia Ora can be found and should be compensated
        - '**[149]** Where fiduciary obligations exist and have been breached, equitable remedies are available both to uphold the principle of undivided loyalty which equity demands of fiduciaries and to discourage others, human nature being what it is, from falling into similar errors.'
        - '**[150]** The fiduciary must make good any breaches arising from its default in discharging the fiduciary obligations. It must account for any profits it has made as a consequence. The overall purpose of the law of fiduciary obligations is to restore the beneficiary to the position it would have been in if the fiduciary had complied with its duty.'
        - '**[151]** In affording remedies for a fiduciary's breach of its obligations, equity is seen, depending on one's point of view, at its "flexible pragmatic best (or worst)."'
            - 'There are, of course, limits. They are those appropriate to enforcing the obligations of conscience. In a proper case, they will require just counter-entitlements to be set off, or deducted, where this can be done with accuracy. The purpose of equity's relief is not punishment but restoration. The "cardinal principle of equity [is] that the remedy must be fashioned to fit the nature of the case and the particular facts".' (*Warman*)
            - Equity is concerned not only to compensate the plaintiff but to

enforce the trust which is at its heart: McLachlin J in *Canson Enterprises Ltd v Boughton & Co*
- This means that equitable damages will often be greater than common law damages

- If Pilmer had adhered to its obligations, and not acted for Kia Ora in producing the report, 'some other firm of chartered accountants would have been retained who, performing their functions independently and objectively would have been bound on the accepted evidence to report that the price of the shares proposed was *not* a "fair" one within ASX rule 3J(3). Or, in the exigencies, it would have been impossible for the protagonist directors to have obtained a report as required by the rule at all. In either event the requirements for shareholder approval would not have been fulfilled'
- Kia Ora might also have sought informed consent from the shareholders; however, it is 'inconceivable' that the shareholders would have given it
- Consequently, Kia Ora would not have been able to proceed with the takeover
- It 'would not have paid the cash and issued the shares'

- The amount of equitable compensation should not be reduced for contributory negligence
  - Likelihood of further impropriety on the part of Kia Ora's directors
    - The Full Court reduced compensation on the basis that Kia Ora's directors probably would have dissipated the company's funds in some other fashion anyway
    - This is not a valid basis for reduction
    - Interest should be awarded for the full term, not just for six months after the takeover, even though this figure is very large as a result
  - Contributing fault
    - There is no authority on whether a concept of reduction for 'contributing fault' can be grafted onto the principles governing equitable remedies
    - '**[170]** Furthermore, all equitable and legal principles must today operate in a universe dominated by the star of statute. It would be surprising if the gravitational pull of statute, felt everywhere else in the law, did not penetrate into the expression and re-expression of non-statutory rules.'
    - Handley: 'Equity has not hitherto considered that a beneficiary is bound to protect himself against his fiduciary. The relationship is not at arm's length and the beneficiary is entitled to place trust and confidence in the fiduciary. The basis for a finding of contributory negligence is therefore lacking.'

<u>Decision</u>

- There was no relevant fiduciary duty capable of being breached (Kirby J dissenting)
- However, Duke Group is nevertheless entitled to damages for breach of contract and negligence, in the amount of $26 178 135.81 (being the amount outlaid for shares in Western United), less the actual value of the shares it received (being $6 439 339), plus damages for interest and loss of use
- Essentially, the majority reasons as follows (though admittedly not in these terms):
  - Fiduciary obligations exist if there is a relevant undertaking (*Hospital Products*, though not expressly mentioned, should, respectively, have been so mentioned)
  - Here, there is no basis for an undertaking because the statutory listing rule spoke simply of a request and report

    - Even if there were fiduciary duties owed, the two alleged conflicts are insufficiently serious to have amounted to breaches
    - Consequently, no fiduciary obligations are owed by Pilmer to Kia Ora
- Kirby J:
    - Recovery in equity would far exceed that awarded at common law, if Kia Ora's claim against Pilmer was framed in contract or negligence
    - Kia Ora should therefore be relieved of the election to take its judgment on the claim framed in contract, and the equitable remedy should be awarded
    - Otherwise, Lord Esher MR's 'famous dictum' would be contradicted:
        - ('any proposition the result of which would be to shew that the Common Law of England is wholly unreasonable and unjust, cannot be part of the Common Law of England')
        - 'The same, I believe, is true of the common law of Australia, as now declared by this [C]ourt. With all respect, I regard the result reached by the majority in this appeal as invoking this dictum.'

As a result of *Pilmer v Duke*, it must now be doubted whether fiduciary duties can exist in the absence of a 'real and sensible possibility' of conflict or unauthorised profit. The relevant enquiry is thus as follows:

(a) **Is there an undertaking by X to act in Y's interests?**
If so, a fiduciary duty will exist within its scope and ambit (see also Kirby J's list of factors); and

(b) **If so, has it been breached?**
Breach will only occur if there is a recognised conflict or profit:

(i) Is there a 'real and sensible possibility' of conflict between the interests of X and Y?
(ii) Has X made an unauthorised profit from his or her position as fiduciary?

Pilmer v Duke makes two things clear (whilst plunging into haphazard confusion a great many others). First, there is now a higher threshold for conflict: more is required than the mere 'possibility' of conflict that has been required since *Keech v Sandford* (and most recently reiterated by Deane J in *Chan v Zacharia*). What is now required is a 'real and sensible possibility' of conflict. The words 'real' and 'sensible' act as qualifiers on a standard of probability, raising it beyond the level of 'possibility' to something more serious or pronounced. In essence, trivial conflicts — such as the expectation of future work, and personal friendship with a client — will be insufficient to amount to breach of duty.

Second, and more implicitly, only certain interests are relevant to the issue of undertaking, and only those same interests appear relevant to the issue of breach. Thus, an undertaking to protect a non-financial interest (eg, bodily integrity) may not be cognisable in equity for the purpose of creating fiduciary relations. Similarly, a conflict between personal, non-financial interests will not amount to a 'real and sensible possibility of [cognisable] conflict'. *Pilmer v Duke* thus suggests that what is required is conflict between *financial* or *economic* interests.

Justice Kirby made some interesting comments about the 'viability of [the] supposed dichotomy [between proscriptive and prescriptive duties]': at [128]. His Honour noted that 'omissions frequently shade into commissions', making it difficult to separate the two kinds of duties. Indeed, this must be accepted as true: a negative duty not to bring into a being a situation of conflict, or a real and sensible possibility of conflict, must entail positive duties to say 'no' to the kinds of associations that would have a tendency to create such conflicts. Similarly, a positive duty to disclose medical records — of the kind unsuccessfully alleged in *Breen v Williams* — must entail a negative duty not to retain or conceal private records from the patient. The difference in quality is really one of articulation rather than any fundamental difference in principle between 'proscription' and 'prescription'.

The dichotomy becomes further eroded when it is remembered that equity already recognises fiduciaries to owe positive (prescriptive) duties. For example, trustees owe many positive duties (to invest, to manage trust property, *et cetera*), which — although strictly incidents of their duties as trustees, rather than fiduciaries — illustrate that equity is willing to impose prescriptive duties onto persons in the position of fiduciaries — indeed, the very *archetype* of the fiduciary.

Regardless of the continued validity of the prescriptive–proscriptive dichotomy, Australian courts remain unwilling to enforce prescriptive or positive duties upon fiduciaries. The majority judgments in *Pilmer v Duke* confirm this.

2 *Prescriptive*

Norberg v Wynrib was one of a series of Canadian cases to adopt a prescriptive model of fiduciary obligations.

***Norberg v Wynrib* (1992) Canada SC:**

Facts
- Mrs Norberg becomes addicted to a painkiller after being prescribed the drug in connection with a series of headaches
- She seeks out Dr Wynrib to obtain access to the drug, at first devising excuses (broken ankle, headaches, etc), but eventually Dr Wynrib discovers her addition
- He offers to provide her with the drug in exchange for 'sexual favours'
- She becomes depressed, quits her job, and commences proceedings in tort (negligence, battery), on a contract (treatment) and for breach of fiduciary duty
- Dr Wynrib argues that she voluntarily consented and was ultimately responsible for her own harm

Issue
- Is Dr Wynrib liable for breach of fiduciary duty?

Reasoning
- Majority:
  - Unnecessary to consider breach of fiduciary duty because battery and negligence have already been made out

- Sopinka J:
  - The scope of fiduciary duties should not be extended for remedial reasons
    - '[Breach of duty] arises out of the relationship of doctor–patient which is essentially based on contract. Breach of the duty can be the subject of an action in either contract or negligence. While undoubtedly, as is the case of lawyer and client, this relationship in some of its aspects involves fiduciary duties, not all facets of the obligations are fiduciary in nature'
    - 'Fiduciary duties should not be superimposed upon [contractual and tortious] common law duties simply to improve the nature or extent of the remedy'
    - Agrees with McEachern CJ:

            - 'If the defendant breached a duty to the plaintiff in this case it was a breach of the duty which a physician owes to his patient o treat her professionally and, unless the breach relates to an improper disclosure of confidential information or something like that, it adds nothing to describe the breach as a fiduciary one'
        - 'The breach of duty alleged here is the obligation of a physician to treat the patient in accordance with standards in the profession'
        - However, this is not a duty founded in fiduciary law, but is rather an obligation arising from contract and tort

- McLaughlin J:
    - There is no liability in tort or contract (*turpa ex causi*)

    - There is a clear fiduciary relationship between a doctor and their patient because of the power relationship that exists between them

    - Fiduciary law recognises the wrong of exploitation in this context
        - 'Only the principles applicable to fiduciary relationships and their breach encompass it in its totality. In my view, that doctrine is clearly applicable to the facts of this case on principles articulated by this [C]ourt in earlier cases. It alone encompasses the true relationship between the parties and the gravity of the wrong done by the defendant; accordingly, it should be applied.'

    - The doctor–patient relationship is fiduciary
        - The patient 'entrusts' their personal information to the physician for medical purposes
        - The patient must inevitable place 'trust and confidence' in the physician
        - The relationship 'shares the peculiar hallmark of the fiduciary relationship — trust, the trust of a person with inferior power that another person who has assumed superior power and responsibility will exercise that power for his or her good and only for his or her good and in his or her best interests.'
        - Fiduciary law is a workable analytic model because it accurately describes the relationship and provides a mechanism to hold physicians to the high standards required by such trust

    - The content of the fiduciary obligation is a duty of loyalty to the patient (which encompasses the narrower negative duties)
        - The ambit of the fiduciary obligation is conceptually distinct from contract and tort, but may overlap in application
        - 'The essence of a fiduciary relationship … is that one party exercises power on behalf of another and pledges himself or herself to act in the best interests of the other.'
        - 'The beneficiary entrusts the fiduciary with information or other sources of power over the beneficiary, but does so only within a circumscribed area, for example, entrusting his or her lawyer with power over his or her legal affairs or his or her physician with power over his or her body.'
        - 'The fiduciary relationship has trust, not self-interest, at its core'
        - Further, '[a] relationship may properly be described as "fiduciary" for some purposes, but not for others. So the question must be asked, did a fiduciary relationship exist between Dr Wynrib and Ms Norberg? And assuming that such a relationship did exist, is it properly described as fiduciary for the purposes relevant to this appeal?'

- ‘Dr Wynrib was in a position of power vis-à-vis the plaintiff; he had scope for the exercise of power and discretion with respect to her. He had the power to advise her, to treat her, to give her the drug or to refuse her the drug. He could unilaterally exercise that power or discretion in a way that affected her interests. And her status as a patient rendered her vulnerable and at his mercy, particularly in light of her addiction.’
- ‘All the classic characteristics of a fiduciary relationship were present.’
- ‘[Dr Wynrib] pledged himself — by the act of hanging out his shingle as a medical doctor and accepting her as his patient — to act in her best interests and not permit any conflict between his duty to act only in her best interests and his own interests — including his interest in sexual gratification — to arise.’
- ‘What will be wrong is if the risk inherent in entrusting the fiduciary with such power is realised, and the fiduciary abuses the power which has been entrusted to him or her.’
- ‘Wilson J went on to state [in *Frame*] that fiduciary duties are not confined to the exercise of power which can affect the legal interests of the beneficiary, but extend to the beneficiary’s “vital non-legal or ‘practical’ interests”. This negates the suggestion inherent in some of the other judgments which this case has engendered that the fiduciary obligation should be confined to legal rights …’
  - Cf, in Australia, *Breen v Williams*; *Pilmer v Duke*
- Thus, for example, in *Reading v Attorney–General*, British soldier who smuggled items past Egyptian guards as a soldier was held to be in breach of fiduciary duty owed to the Crown
  - The Crown’s interest was a ‘practical’ or ‘moral one’, ‘namely, that its uniform should not be used in corrupt ways. The soldier–fiduciary had no power to change the legal position of the British Crown…’
  - Wilson J in *Frame*: ‘In my view, what was protected in that case was not a “legal” interest but a vital and substantial “practical” interest’
- Here, Norberg seeks protection of a non-traditional interest: ‘ensuring that the power entrusted to physicians by us, both collectively and individually, [is] not to be used in corrupt ways, to borrow the language of *Reading v Attorney–General*’
- ‘The Hippocratic Oath reflects this universal concern that physicians do not exploit their patients for their own ends, and in particular, not for their own sexual ends’
- ‘The interests which the enforcement of these duties protect are, to be sure, different from the legal and economic interests which the law of fiduciary relationships has traditionally been used to safeguard.’
- Wilson J in *Frame*: ‘To deny relief because of the nature of the nature of the interest involved, to afford protection to material interests but not to human or personal interests would, it seems to be, be arbitrary in the extreme’

o The fact that Norberg obtained and used drugs improperly is not a bar to her claim in equity
  - In equity, the moral conduct of the plaintiff is examined, as reflected in the maxim, *he who comes into equity must come with clean hands*
  - At common law, this is embodied in the doctrine of *ex turpi causa non oritur actio*
  - Whether Norberg did anything wrong must be assessed in the context of

her relationship with Dr Wynrib
- ‘She was not a sinner, but a sick person, suffering from an addiction which proved to be uncontrollable in the absence of a professional drug rehabilitation program[me]’
- ‘“hustling” doctors for drugs is a recognised symptom of her illness’
- In light of the seriousness of the breach, the clean hands maxim is little other than ‘blaming the victim’
- Consequently, her conduct will not be viewed as improper such as to prevent her coming into equity

- Dr Wynrib breached is duty to Ms Norberg in several respects
  - ‘It is not disputed that Dr Wynrib abused his duty to the plaintiff. He provided her with drugs he knew she should not have. He failed to advise her to enrol in an anti-addiction program[me], thereby prolonging her addiction. Instead, he took advantage of her addiction to obtain sexual favours from her over a period of more than two years.’
  - ‘[Dr Wynrib] maintained control of the relationship … not by retaining a professional attitude and treating Ms Norberg as the sufferer of a serious illness who needed his help, but by exploiting his knowledge, position and the power they gave him over her to coerce her to satisfy his sexual desires. A more grievous breach of the obligations, legal and ethical, which he owed her as his patient can scarcely be imagined.’
  - No decision is reached whether ‘any and all sexual contact between a doctor and his patient is a breach of the doctor’s fiduciary obligation’
  - (However, relevant Canadian medical standards state that ‘any’ sexual contact between doctor and patient is a ‘sexual violation’ punishable by revocation of the doctor’s practising licence for five years)
  - ‘where such a power imbalance [as that between doctors and their patients] exists it matters not what the patient may have done, how seductively she may have dressed, how compliant she may have appeared, or how self-interested her conduct may have been — the doctor will be at fault if sexual exploitation occurs’

- Sopinka J’s objection that treating the case as one of breach of fiduciary duty adds noting to the remedies already available to the plaintiff is not insurmountable
  - ‘What is really at issue here is the scope of the fiduciary obligation. The majority of the Court of Appeal and Sopinka J would confine it to matters akin to the duty not to disclose confidential information, the situation dealt with in *LAC Minerals*. If that restriction is accepted, then they are right; there is little reason to refer to it in this case. But I do not think that narrow view of the scope of the fiduciary obligation is correct.’
  - ‘The principles … are of general application, translatable to different situations and the protection of different interests [to] those hitherto recognised. They are capable of protecting not only narrow legal and economic interests, but can also serve to defend fundamental human and personal interests, as recognised by Wilson J in *Frame v Smith*.’
  - Breach of duty allows bars to recovery to be overcome (such as *ex turpi causa*, mitigation), and holds fiduciaries to higher standards than those to which they otherwise would be bound under tort and contract law
  - ‘My colleagues, with respect, strain to conclude the contrary’

- A more generous remedy should be imposed because equity imposes higher standards of conduct than tort or contract

- Equity has more flexible remedies that can be moulded to deliver justice
- Those remedies reflect the nation that the fiduciary should take bear responsibility for their wrong
- Here, Mrs Norberg suffered pain, suffering and embarrassment; equitable compensation should be awarded, including punitive damages
  - The quantum of this remedy is higher than at common law
- Dr Wynrib's behaviour is described as reprehensible
- Examines a report by a medical association suggesting that sexual exploitation by doctors is widespread
- The wrongdoer, Dr Wynrib, should be punished to express disapproval for his conduct and to deter other doctors, thereby reinforcing the standards of behaviour expected of doctor fiduciaries
- The doctrines of tort and contract do not capture the essential nature of the wrong done here: in contract and tort, the parties are independent
- Fiduciary duties may also be superimposed upon contractual and tortious duties: fiduciary law has trust, not obligations, at its core
- Vulnerability is essential and fundamental to all fiduciary relationships
- The Court has a role to play in expanding the categories of interests protected by fiduciary law; the Court should not adopt a closed, commercial view of fiduciary relationship

- This doesn't fit well with the proscriptive approach
  - Sexual harm is unlikely to be recognised by the High Court of Australia
  - No financial conflict of interest: emotional/professional conflict
  - See Federal Court sexual abuse case in guardian–ward
  - Perhaps 'no conflict, no profit' will be interpreted more broadly: doctor abusing/not treating a patient to pursue his or her own personal interests
  - Tort law is still likely to provide a remedy, but it won't be as large, and may not provide the necessary degree of flexibility (eg, proprietary rights)
  - A fiduciary claim may also alleviate a statute of limitations bar (note that the equitable doctrine of laches may pose a difficulty for plaintiffs, though it does afford considerably greater flexibility)

<u>Decision</u>

- Majority:
  - Tort of battery is made out
  - There was no consent
  - She was not acting improperly such as to reduce liability
  - Award $30k total damages

Norberg v Wynrib was later applied in the Canadian case of *McInerney v McDonald* (1992) to unanimously find that the fiduciary duty owed by a doctor to their patient encompasses a positive duty to disclose medical records (cf *Breen v Williams*).

A similar approach is reflected by the result in *M(K) v M(H)*, holding that the parent–child relationship is of a fiduciary character.

M(K) v M(H) (1992) Canada SC:

Facts
- A girl is sexually abused by her father from ages 8 to 17
- After extensive counselling, she recognises the abuse and decides to sue her father for breach of fiduciary duty
- It is many years later by the time proceedings are commenced, and the limitation of actions period has expired as against the time at which the abuse was alleged to have occurred

Issue
- Does a fiduciary relationship exist?

Reasoning
- Incest is both a tort and a breach of fiduciary duty
    - For the tort action, the limitation period does not begin to run until the nexus between the abuse and the harm caused is realised by the victim
    - Consequently, neither action is necessarily statute-barred
- It is 'intuitively apparent' that a parent owes fiduciary duties to their children
- McLaughlin J noted that there could be a fiduciary relationship even if there is no unilateral undertaking by the fiduciary
    - Thus, the fact that a parent does not formally or specifically undertake to act in the best interests of their child is no reason not to hold them to the standards and obligations of a fiduciary
    - The vulnerability of children suggests that such a duty must be owed
- Content of the duty:
    - Stated positively, though in the context of avoiding harm to the child (unsurprising given the facts of the case)
    - The positive duty is phrased as a duty of a parent to act in the best interests of their child
    - The negative duty this encompasses and necessarily entails is not to harm the child
- In Australia, it seems unlikely whether the parent–child relationship will be classed as fiduciary
    - However, if there is a financial conflict or profit (eg, taking the child's property) the Court may recognise that the relationship is fiduciary to that extent

Decision
- The girl is granted $50 000 compensation
- McLaghlin and Here-Deubeux JJ note that this award may be inadequate

The issues of *M(K) v M(H)* have not arisen for reconsideration since 1992.

This line of Canadian authority is importance because it illustrates the broader, prescriptive model of affirmative fiduciary liability.

The prescriptive approach offers claimants several benefits:

1 **Wider scope of liability**
A specific duty of loyalty imposes a wider sphere of liability than could be imposed in tort or by contract.

2 **Fewer restrictions**
Statutory restrictions, such as the *Limitation of Actions Act*s, are subject to discretionary removal by a court of equity. (It may well be questioned why different limitation periods ought to apply depending on the jurisdiction — perhaps it is the limitation acts which need reform.)

3 **Remedial flexibility**
Equitable compensation is more generous than common law damages; limiting principles, such as remoteness, mitigation and intervening acts do not apply. Higher awards are also sometimes made to deter breaches of duty (see, eg, MacLoughlin J in *Norberg v Wynrib*).

Detractors of this approach emphasise the uncertainty created by a broad duty of 'loyalty'.

3 *Status of non-financial duties in Australia*

As a result of the proscriptive approach of *Breen v Williams* and *Pilmer v Duke*, it must be doubted whether fiduciary duties can arise in Australia to protect non-pecuniary interests.

Naturally, this would not warrant discussion if the interest affected by the alleged breach was economic in nature. It would be sufficient to adopt the traditional arguments, referring to vulnerability, trust and confidence, and like tests to determine the existence of a relationship. Its existence may even be presumed as a matter of equity.

The prospective and prescriptive approaches are primarily relevant to the determination of claims at the fringes of fiduciary law. Issues of non-financial duties arise in the context of non-financial harm, such as sexual abuse or a positive duty to inform. In these borderline cases, it is essential to have regard to the tension between prescriptive and proscriptive approaches.

Following *Breen*, the doctor–patient relationship, insofar as it can inflict economic harm to the patient, is generally not fiduciary. However, it can become fiduciary in some circumstances. The boundaries of the proscriptive approach would need to be examined to determine when this is so.

If the relevant undertaking and vulnerability exists, and both financial and non-financial harms are caused to the principal, both approaches might be argued to apply. The financial loss would be compensable by the traditional fiduciary approaches. The other non-financial loss would probably be limited, in Australia, to recovery in tort or on the contract.

E *Fiduciary Duties of the Commonwealth*

1 *Duties with respect to indigenous land rights*

The issue of whether the Crown owes fiduciary duties to its subjects, or (in less synecdochic terms) the state to its citizens, most often arises in relation to wrongs committed against the indigenous population during colonisation.

In the United States of America, courts have dealt with this issue plainly in favour of the indigenous inhabitants of the land. At least since *Cherokee Nations v Georgia* (1831), American courts have accepted that the state is a fiduciary with respect to the indigenous population. According to Marshall CJ, the United States of America owes fiduciary duties to native Americans as trustee of their land, managing it on their behalf. Although his Honour's judgment is phrased in historically quaint but culturally condescending terms (referring to 'Indians' as the 'dependent domestic nations'), the principle of state-owed fiduciary duties has long been accepted.

In Canada, fiduciary duties are also recognised as flowing from the state's position as occupier of native land: *Guerin v The Queen* (1984). In that case, the state was in breach of duty by rending native British Columbian land for profit.

The issue was first dealt with in comprehensive terms in Australia by *Mabo v Queensland [No 2]*, where Toohey J considered whether the Commonwealth's capacity to extinguish indigenous land rights gave rise to fiduciary duties:

Mabo v Queensland [No 2] (1992) HCA:

Issue

- Does the state owe fiduciary obligations with respect to land rights?

Reasoning

- Toohey J:
    - Extinguishment of native title by the Crown amounts to breach of fiduciary duty
        - This creates a right to compensation

    - A fiduciary obligation arises from the power of the Crown to extinguish native title
        - This vulnerability to extinction gives rise to the obligation
        - Even if the power to extinguish is not enough to found a fiduciary obligation, the government policy of protecting indigenous land rights shows an undertaking to act in the interests of the indigenous peoples
            - 'it is, in part at least, precisely the power to affect the interests of a person adversely which gives rise to a duty to act in the interests of that person; the very vulnerability gives rise to the need for the application of equitable principles…'
            - '…a policy of "protection" by governing emerges from the legislation … as well as by executive actions such as the creation of reserves …'
            - This suggests an undertaking to protect indigenous interests
            - (As a matter of fact, this may not be entirely accurate: some have gone so far as to describe it as 'a[n] historical lie')
        - 'Be that as it may, if the Crown in right of Queensland has the power to alienate land the subject to of the Meriam people's traditional rights and interests and the result of that alienation is the loss of traditional title, and if the Meriam people's power to deal with their title is restricted in so far as it is inalienable, except to the Crown, then this power and corresponding vulnerability give rise to a fiduciary obligation on the part of the Crown. The power to destroy or impair a people's interests in this way is extraordinary and is sufficient to attract regulation by Equity to ensure that the position is not abused. The fiduciary relationship arises, therefore, out of the *power* of the Crown to extinguish traditional title by alienating the land or otherwise; it does not depend on an exercise of that power.'

    - Conflicts of interest can readily arise having regard to state governments' plenary powers; however, inconsistent conduct by the Crown will amount to a breach of duty in respect of which a proprietary remedy may issue in favour of the affected indigenous people
        - 'A fiduciary has an obligation not to put himself or herself in a position of conflict of interests. But there are numerous examples of the Crown

exercising different powers in different capacities. A fiduciary obligation on the Crown does not limit the legislative power of the Queensland Parliament, but legislation will be a breach of that obligation if its effect is adverse to the interests of the titleholders, or if the process it establishes does not take account of those interests.'

Two foundations for the fiduciary duty were identified in *Mabo*:

- **Vulnerability**
  Aborigines are vulnerable to the acts of the Crown, and so warrant protection in equity;

- **Undertaking**
  Queensland's history evidences an intention by the Crown to protect the land of indigenous peoples in certain respects.

The issue again arose for consideration in *Wik Peoples v Queensland* ('*Wik*'). *Wik*, along with later cases, were more reluctant to recognise fiduciary duties of this kind. Brennan CJ, in particular, expressed doubts about whether fiduciary principles apply.

Wik Peoples v Queensland **(1996) HCA:**

Issue
- Does the grant of a pastoral lease extinguish native title?

Reasoning
- Brennan CJ (dissenting):
  - The Crown does not owe a fiduciary duty to indigenous people
  - For the undertaking approach to succeed, there must be identified some action capable of identifying the beneficiary's interests; *and* it must be reasonable for the fiduciary to expect the fiduciary to act in their interests
  - Although the Crown has power to extinguish native title, this does not give rise to a fiduciary duty because it is necessarily exercised against the interests of native title holders
  - This means that the indigenous population cannot expect the state to act in their interests (since the power it holds is inevitably to be used against them)
  - Thus, the mere existence of a capability to extinguish native title, such that the capability must be put to that purpose alone, is sufficient to negate the existence of a fiduciary relationship
  - Cf Toohey J: the grant can benefit aborigines
  - The grant *does* extinguish native title

Decision
- Whether there is extinguishment depends on the term of the grant: in the event of inconsistency of terms, the grant prevails

It is probable that statutory intervention in the form of the *Native Title Act 1993* (Cth) was what dampened the initial judicial enthusiasm for the analytic structure provided by fiduciary law in the context of indigenous land rights. By imposing a comprehensive regime of land regulation and compensation, there was no longer the same level of vulnerability as that which existed prior to

1992. As a result, it is unlikely that any future claim brought by an indigenous plaintiff predicated solely on breach of fiduciary duty will be successful in Australia.

2 *Duties with respect to the stolen generation*

Cubillo and Gunner v Commonwealth (‘*Cubillo*’) concerns a guardian–ward relationship. The issue was whether the state, as a guardian for indigenous children during the ‘cultural assimilation’ (stolen generation) programme, was liable for breach of fiduciary duty to those children who were forcibly removed from their parents.

The Federal Court of Australia held that claims arising out of tort, contract and fiduciary duty should all be rejected. However, the fiduciary character of the relationship between state–guardian and indigenous child–ward was accepted.

Cubillo and Gunner v Commonwealth (2001) FCA:

<u>Issue</u>

- Did the practice of cultural assimilation amount to the breach of a fiduciary duty owed by the Crown to indigenous children?

<u>Reasoning</u>

- The plaintiff argued that a fiduciary relationship arises because of the role played by the Commonwealth’s servants and agents in removing children, and because of the Commonwealth’s power over and assumption of responsibility in relation to indigenous welfare
- In the alternative, it was submitted that the directors of the relevant aboriginal welfare service owed fiduciary duties as individuals because they could exercise power over the children’s welfare
- Breaches:
    - It was also argued that the failure to meet the relevant limitation period was caused by the Commonwealth’s failure to inform them of their rights to legal redress
    - The Commonwealth did not act in the children’s best interest by using them as labour in white homes and encouraging assimilation
    - The Commonwealth had created a conflict of interest by undertaking to care for the children and pursuing its policy of assimilation

- Trial judge:
    - Disagrees with the ‘conflict’ and ‘best interests’ arguments on the facts, citing *Paramasivam v Flynn* as binding authority for limiting the duties of a fiduciary to the ‘no conflict’ and ‘no profit’ rules
    - It would therefore be inappropriate to expand the nature of fiduciary duties beyond these rules to go beyond protecting economic interests
    - Consequently, there was no fiduciary duty
    - Even if there was, the action was barred in equity by the doctrine of laches; it would be inequitable and unreasonable to place the defendant where they had to defend a claim so many years after the alleged events (lost witnesses, evidence)

- Full Court of the Federal Court of Australia:
    - The fact that one person may be a fiduciary does not mean that all aspects of a relationship between them and the other may be covered by equitable principles
    - It is true that the directors of the Department of Indigenous Affairs were the

guardians of the stolen children
  - It is true that the guardian–ward relationship is fiduciary
  - However, this does not mean that all aspects of that relationship are fiduciary
  - Fiduciary duties cannot be imposed so as to conflict with contract and tort
    - Because of the fiduciary claim is coextensive with the tort claim, it is within the purview of tort law and there is no room for the imposition of fiduciary duties
    - This means that: if a party alleges that X is tortious conduct, they cannot allege that X is also a breach of fiduciary duty
    - This is a very narrow, proscriptive approach
  - In any event, the doctrine of laches would apply

Decision
- Common law grounds of relief fail
- An application for special leave to appeal to the High Court was refused on the basis that, having regard to the laches argument, it was not an appropriate forum in which to litigate the issue

Effectively, the Court reasoned that the claim should be rejected because the alleged duty (to protect the familial and cultural interests of the children and to act in their best interests) did not fit the known mould of fiduciary duties. This decision reinforces the fact that fiduciary law protects measurable economic and financial interests, not bodily, mental, personal or cultural interests.

F *Guardian–Ward*

A person entrusted with the care of another is known as a guardian. The person for whom they care (their ward) is in a fiduciary relationship with the guardian (*Hospital Products*).

Consequently, it has been held that sexual assault by a guardian of his ward gives rise to an action for breach of fiduciary duty: *Paramasivam v Flynn*; *Cubillo v Commonwealth* (Full Court of the Federal Court; not overturned on appeal).

Paramasivam v Flynn (1998) FCA:

Facts
- In 1976, the defendant said to the plaintiff that he would support her son through school in Fiji
- The plaintiff was 14 years old at this time, and alleged sexual abuse by the defendant
- In 1981, the defendant paid for the plaintiff to come to Australia and become his official guardian
- Throughout 1981–1986, the plaintiff alleges several instances of sexual abuse; during this time, the defendant threatened to return him to Fiji or withhold his passport
- In 1986, the plaintiff brought an action for the tort of assault and breach of fiduciary duty
- In an interlocutory proceeding, the defendant objects on the basis of lapse of time

Issue
- Is there any real prospect of success for the substantive (ie, fiduciary) claim?

Reasoning

- Factual problems
- There was a lack of particularity about the times and places when and at which the abuses allegedly took place
- The alleged abuse cannot be corroborated by any third party (though this is somewhat typical of these types of claims)
- Doctrinal issue
- The plaintiff has not attempted to define the circumstances giving rise to the fiduciary duty, or to definite its scope or content
  - This is despite the fact that the guardian–ward relationship is a category one relationship of presumed fiduciary obligations
  - Subsequent cases have reaffirmed this status
  - However, the Court notes that not all guardian–ward relationships will be fiduciary
  - Indeed, the Court observes that 'the plaintiff's claim is novel under Australian law because it only protects economic interests under fiduciary law. The conduct complained of here relates only to tort law, and … to allow [equity] to enter would be to allow a leap in conventional legal reasoning.'
  - Applies *Breen v Williams*

<u>Decision</u>

- No, there is no real prospect of success
- Consequently, the statute bar will not be obviated and the trial cannot be brought

In *Paramasivam*, the Federal Court explicitly disapproved *M(K) v M(H)* (a case concerning parent–child fiduciary relationships).

II *Obligations of Fiduciaries*

A *Summary of Obligations*

If a fiduciary relationship is found to exist, certain obligations attach to the person in the position of fiduciary. The content of these obligations is as follows:

1. **Conflicts are bad**
The fiduciary's interest and duty must not be placed in conflict (*Chan v Zacharia*); thus, a fiduciary cannot normally buy property from the principal except with full disclosure (*McKenzie v McDonald*);

2. **Fiduciaries must not generally profit**
The fiduciary must not benefit from the conduct that it has been asked to perform by the principal (*Hospital Products*); this is so even if the fiduciary thereby enables the principal to obtain some benefit which it could not otherwise have obtained (*Boardman v Phipps*);

3. **Fiduciaries can profit when allowed**
The fiduciary may reap a profit with the knowledge and informed consent of the principal, providing disclosure is sufficient (*Boardman v Phipps*);

4. **Good intentions will not suffice**
Even if a fiduciary has altruistic motives, they may still commit equitable fraud (*Nocton v Lord Ashburton*; *Boardman v Phipps*);

5. **Fiduciaries must pay up**
The fiduciary is liable for profits derived from knowledge or other opportunities afforded by their position (ie, caused to be possible);

6. **Fiduciaries must not cause loss**
The fiduciary must generally not cause loss to the principal; however, they will not be in breach simply for negligently failing to disclose or obtain relevant information (*BLB Corp of Australia v Jacobsen*);

7. **Failing to cause loss is no answer**
The fiduciary will be liable for a breach of these duties notwithstanding that their conduct did not cause loss to the principal (*Whitehouse v Carlton Hotel Pty Ltd*); and

8. **Fiduciaries must be fair**
Where there is more than one principal, the fiduciary must not favour one over another but must instead exercise their powers fairly (*Whitehouse v Carlton Hotel Pty Ltd*).

B *No Conflict, No Profit*

Of the above rules, two are by far the most important. A fiduciary must account to the principal for any benefit or gain that is obtained or received:

(i) in circumstances where there is at least a significant possibility of conflict between his fiduciary duty and his personal interest in the gain ('the "no conflict" rule'); or

(ii) by use of (or by reason of) his position as fiduciary, or of opportunity or knowledge resulting from it ('the "no profit" rule').

Any such benefit or gain is held on constructive trust for the principal (*Chan v Zacharia*).

Chan v Zacharia (1984) HCA:

Facts

- *Chan v Zacharia* concerns a fiduciary relationship between two partners in a former medical clinic
- The partnership was determined and wound up because they could not agree on whether to exercise an option of renewal in their lease agreement
- The partner, Dr Chan, decided to exercise the option independently, and obtained for himself an extension of the clinic lease
- The other partner, Dr Zacharia, sought a declaration that Dr Chan is bound to account for any profit he receives under the new lease

Issue

- The parties are clearly in a fiduciary relationship
    - The two doctors hold legal rights under the lease, including the option to renew, as trustees to the extent the other is entitled to share in the proceeds of the realisation of partnership assets
    - Drs Chan and Zacharia were each both trustees (of the legal rights) and beneficiaries (under the partnership) of those rights
- What, then, is the content of that relationship?
    - Specifically, is Dr Chan obliged to pay Dr Zacharia the result of any profits obtained after the dissolution of the partnership?
    - Or, alternatively, is Dr Chan 'entitled to decline to join in an exercise of the option for a further lease and to obtain and retain the benefit of a new lease of the premises for himself'?

Reasoning (Deane J)

- Each party was obliged as fiduciary to the other to act in the interests of the dissolved partnership and the beneficial realisation of its assets
    - The fiduciary relationship persists until the assets have been distributed
    - This suggests that ex-partners may have ongoing fiduciary obligations towards one another
    - The fiduciaries will be held to account for any personal gain

- There are several particular formulations of the rule requiring fiduciaries to account for personal gain; in general, however, they embody two themes:
    - First, the fiduciary must pay an account of profits to the principal where they obtain a gain in circumstances where there is at least a possibility of a conflict between their interests and the fiduciary duty
        - That is, he should be discouraged from creating a conflict between his personal interests and those of the principal
        - A 'significant possibility' of conflict is sufficient; certain and actual conflict is unnecessary
        - This is a higher standard than that adopted by the House of Lords in *Boardman v Phipps* ('mere possibility'), amounting to a more lenient test for fiduciaries
        - Note also *Pilmer v Duke*, which framed the issue in terms of a 'real or substantial possibility of conflict' (likely to be a similar standard)

        - [Note the likelihood of different constructions of the facts: cf Murphy J: discuss how the facts might be thought to demonstrate a significant or substantial possibility of conflict]
        - [Note: conflict must also be within the scope of the fiduciary duty: cf other contexts: "betting advice at a party vs legal advice in an office"]
        - If the conduct falls within the scope of the fiduciary relationship, then go on to consider whether there is conflict or profit; otherwise, however, there can be no breach; if there is a conflict or profit, ask 'has there been fully informed consent?'
    - Second, the fiduciary must account for any gain obtained as a result of opportunities (including knowledge) presented by his position
        - That is, he should be prevented from misusing his position to obtain a personal advantage

- The rule binding fiduciaries is as follows:
    - A fiduciary must account to the principal for any benefit or gain that is obtained or received:
        - (i) in circumstances where there is at least a significant possibility of conflict between his fiduciary duty and his personal interest in the gain; or
        - (ii) by use of or by reason of his position or of opportunity or knowledge resulting from it.
    - Any such gain or benefit is held by the fiduciary as constructive trustee for the principal (*Keith Henry & Co Pty Ltd v Stuart Walker & Co Pty Ltd* (1958) HCA)
    - It is immaterial that the fiduciary acted in good faith
    - It is immaterial that no loss or damage was caused to the principal

- When does the constructive trust arise?
    - When there is an actual breach of fiduciary duty
    - When will this occur?
        - (Normally) When the fiduciary pursues their interest or misuses their fiduciary position for personal gain
        - (Sometimes) Only when the fiduciary, having made a personal gain, fails to account to the principal for it (eg, receipt of a payment, which is then forwarded to the principal: no breach)

- A trustee of a tenancy who obtains a renewal for himself holds the interest as part of the trust estate (*Keech v Sandford* (1726) UK)
    - Consequently, an irrebuttable presumption arises that any rights obtained by Dr Chan in respect of the lease were obtained by means of his position as trustee of the previous tenancy; and
    - There is a rebuttable presumption of fact that the rights were obtained by use of his position as a partner in the dissolved partnership
    - (Ie, it is possible for a single benefit to be obtained by the use of two distinct fiduciary positions)

- Exception: if the document or instrument creating the fiduciary relationship allows the fiduciary to act as he did, he will not be in breach of his duty to act in that way
    - There must be 'informed and effective consent' of the principal

- Dr Chan obtained the lease through his position as fiduciary
    - On the facts, Dr Chan was introduced to the premises through the partnership
    - Dr Chan therefore holds his rights as tenant as a constructive trustee for the partnership unless there is some reason for refuting the second presumption

- (Ie, the *cestui que trust* is the other partner)

Decision

- Dr Chan will be in breach of fiduciary duty if he does not make an account of profits to Dr Zacharia for benefits obtained under the lease renewal
- Consequently, Dr Chan holds his interest under the lease on constructive trust for the partnership, and it forms an asset to be considered during its winding up

C *Additional Considerations*

The fact that a principal was never in a position to make the impugned profit themselves is irrelevant. A fiduciary will be in breach of fiduciary duty if they make unauthorised profit under any circumstances. This is a longstanding principle of equity, dating back as far as 1726 in the English case of *Keech v Sandford*.

Keech v Sandford **(1726) UK Ch:**

Facts

- A trust is setup to care for a child
- One of the assets held by the trust is a lease
- The trustee attempts to renew the lease on behalf of the trust, but the lessor refuses to sign the lease renewal
- The trustee then decides to take on the lease for himself in his own name
- The beneficiary sues the trustee for breach of fiduciary duty

Issue

- Has the trustee breached their fiduciary obligations?

Reasoning

- If a fiduciary cannot make a profit from their position, then even when the beneficiary is themselves precluded from making a profit, the trustee still cannot go ahead to make that profit
- The principles attaching to fiduciaries are strict obligations; the high standard of conduct is designed to deter improper conduct

Decision

- The trustee's conduct does amount to a breach

Modern cases relax this position somewhat: fiduciaries can profit with permission of the principal (since contractual obligations can coexist with fiduciary obligations (see *Hospital Products* per Mason J). Fiduciaries can profit with respect to some aspects of their relationships, in some circumstances, but not all. However, a blanket ban on profit is inaccurate and inappropriate.

Boardman v Phipps restates in a modern context the rule that profit is prohibited notwithstanding that the principal was in no position to itself benefit from undertaking the impugned conduct itself — even where the principal in fact receives substantial gains as a result of the fiduciary's breach.

Boardman v Phipps **(1967) UK HL:**

Facts
- Boardman is a solicitor; he acts on behalf of an estate as trustee (also a trustee)
- The plaintiff, Phipps, is a beneficiary under that trustee
- Part of the trust's assets includes shares in a company (as minority shareholder)
- The company was poorly managed and not making a profit; consequently, the value of the shares was lower than they could have been
- The trustees intend to change the company's management in order to improve profits and, hence, the share price
- However, they need a majority of shareholders to agree to the change
- The trust itself was not permitted to purchase additional shares because further investment in shares was unauthorised (this restriction was contained in the trust deed)
- Consequently, Boardman makes a takeover bid for the company
- He funds the share purchase with his own money and is successful in gaining control of the company
- Many of the trust's beneficiaries are aware of the takeover, and don't say anything
- Boardman's takeover resulted in all the beneficiaries — including Boardman — making substantial profits
- Boardman was acting in good faith; however, all of the information about the company's management was obtained in the course of his role as trustee of the trust
- Phipps, one of the other beneficiaries, alleges that Boardman profited from his position as trustee in breach of his fiduciary duties

Issue
- Was there a breach of fiduciary duty?

Reasoning
- Majority:
  - A fiduciary can be accountable despite the fact that he acted in good faith, and despite the fact that a fiduciary would not otherwise be able to take the benefit for themselves
  - Nothing short of 'fully informed consent' by the beneficiaries would have permitted Boardman to keep the profit
  - This was not present on the facts
    - At least one beneficiary had dementia and was unable to give consent
    - They were not consulted or told about the takeover
    - The fact that some beneficiaries approved of the takeover is insufficient
    - Must be unanimous
    - If one beneficiary is incapable or unwilling to give consent, there will not have been fully informed consent
  - There was also the possibility of a conflict of interest
    - Mere possibility will be sufficient
    - Eg, Boardman could have used his shares as a tax offset by stripping the company of assets and run it at a loss (not to the benefit of the shareholders)
    - Eg, Boardman could accidentally mismanage the company to the detriment of the beneficiaries
    - Eg, if the trust wanted to vary the conditions so as to enable it to buy more shares, and Boardman did not want to sell any/

- Lord Upjohn (dissenting):
  - Agrees with the basic principles of law, but disagrees as to their flexibility and

application to the facts
- Principles:
    - A fiduciary will not be made to account for profit in every case
    - There must be an actual or potential conflict of interest
    - The fiduciary's conduct must be *capable of injuring* the trust
- Application:
    - Here, Boardman's conduct was incapable of conflicting with the interests of the trust, because the trust was restricted from purchasing additional shares
    - It would therefore be unreasonable and inequitable to hold Boardman liable

Decision
- (3:2) There was a breach of fiduciary duty
- Boardman must account for any profits he made to the trust
- The shares he held would be held on constructive trust for the trust
- However, the Court makes a reasonably generous award to allow for Boardman's time and expenses in completing the takeover

1 *Fiduciary standards*

Chan requires a 'real and substantial' possibility of conflict (rather than any possibility: *Phipps*).

Issue: does *Chan*'s dilution of the 'no profit, no conflict' rules lower the ethical standards expected of fiduciaries. Ie, is the strictness of the *Phipps* standard being undermined to an impermissible extent?

2 *Onus of proof*

The effect of *Chan* and *Phipps* is to place the burden of establishing that fiduciary obligations have not been breached upon the fiduciary. That is to say, that the fiduciary must establish that, for example, their acquisition of property did not derive from or was not occasioned by a breach of the relationship.

D *Impact of Contract*

Issue: is it possible to modify the nature or scope of fiduciary obligations by means of a contract? For example, can a solicitor 'contract out' of the no conflict, no profit rules.

This has not been conclusively resolved by the High Court of Australia.

Lower courts are still grappling with the issue; in particular, they consider whether the English decision of *Armitage v Nurse* (1997), holding that fiduciaries can contract out of all fiduciary obligations except the requirement to act in good faith. Thus, fiduciaries could contract out of the no profit, no conflict duties. The Court said that this would not apply in cases of fraud: thus, if the breach is fraudulent, then an exemption clause will be of no effect. This is consistent with the equitable maxim *fraud unravels everything*.

In the United States America, *Armitage* was applied by the Supreme Court of the United States in *Reader v Fried* (2001) (company superannuation trust; a trustee, also a director of the company, transferred unwanted company property to the trust, but the trust paid too high a price; the trustee could not be protected by an exemption clause purporting to exclude the no profit rule).

If *Armitage v Nurse* is applied in Australia, it will be possible to contract out of most fiduciary obligations except in case of fraud. This is especially troubling. Some commentators have suggested introducing legislation to prevent this.

III *Remedies*

A *Jurisdictional Basis*

1 *Available remedies*

Equity has exclusive jurisdiction to issue remedies for breach of fiduciary duty. This means that common law remedies cannot be awarded to plaintiffs who successfully allege breach of fiduciary duty — to do so would be to engage in the so-called 'fusion fallacy'. Only equitable remedies are available.

2 *Flexibility and discretion*

Equitable remedies are relatively flexible, but only available on a discretionary basis. As a result of this remedial flexibility and judicial discretion, it is often the case that judgments will oscillate between chastising and sympathising with defendants.

B *Types of Remedies*

1 *Personal remedies*

A personal remedy is directed at the person of the defendant. This means that the sanction operates against them as an individual. Equitable compensation is the most common personal remedy. It effectively means that the person against whom damages awarded must pay them to the plaintiff or be liable in the criminal law for contempt of court.

The concealed sanction is normally imprisonment. If the defendant does not comply with the terms of the order, they will go to jail for contempt. A variety of other mechanisms also exist to mandate compliance, such as search and seizure orders.

Personal remedies include:

- Account of profits;
- Equitable compensation; and
- Rectification.

2 *Proprietary remedies*

Proprietary remedies are directed against specific property in which the defendant has title. The essence of such a remedy is transfer of the relevant property to the plaintiff. Thus, in equity, the subject property *belongs* to the plaintiff from the date of the court order conferring the remedy. No secondary sanction is needed for a proprietary remedy because it is secured against the defendant's assets directly.

A proprietary remedy effectively makes the successful plaintiff a secured creditor of the defendant. This illustrates the primary advantage of a proprietary remedy: they are immune from declarations of bankruptcy. It means that the plaintiff will have first priority to the defendant's assets in the event of their insolvency. It also allows the plaintiff to enforce their interest by way of sale of the defendant's assets.

By contrast, a person entitled to a purely personal remedy would find herself in the position of an unsecured creditor, and may only recover a small proportion of their entitlements from the trustee in bankruptcy. Holders of proprietary remedies are in a stronger position because they can enforce their order not only against the defendant but also against their other creditors. The asset the subject of the order will not be divided among the creditors but will be ceded as a matter of priority to the plaintiff.

Proprietary remedies include:

- Charge;
- Lien;
- Constructive trust; and
- Election to take property.

In the event of a dispute between multiple recipients of proprietary remedies, or between multiple secured creditors, a priority dispute arises. The division of assets in these circumstances is governed by the rules of property law.

C *Purposes of Remedies*

Each equitable remedy is appropriate only to certain types of breaches. Whether a given remedy should be sought depends on the particular circumstances of the breach, including its consequence for the fiduciary and principal.

1 *Compensating loss*

(a) Equitable compensation

If the principal suffers loss as a result of the fiduciary's breach of duty, it will normally seek equitable compensation. The award of compensation fulfils the purpose of obviating the principal's loss by way of ordering the fiduciary to make recompense. This is, however, a personal remedy.

There is no equivalent proprietary remedy designed to compensate loss. This leaves plaintiffs dependant on the defendant's solvency for success.

This remedy should be sought when the principal's loss exceeds the defendant's gain from the breach.

2 *Disgorging gains*

(a) Account of profits

If the breach does not cause loss to the principal *per se*, but enables the fiduciary to reap a substantial profit, then the principal may seek an account of profits. This means that the fiduciary must deliver unto the principal any profits obtained as a result of their breach of duty.

It matters not whether the fiduciary retains or has since lost those benefits, except insofar as the defendant's insolvency might prevent the plaintiff from obtaining full recovery of those gains.

(b) Constructive trust

Alternatively, the Court may make an order of constructive trust. This is an order that the fiduciary hold specific, identified property on trust for the beneficiary. Effectively, the fiduciary is deemed to have transferred that property to the beneficiary.

For example, in *Boardman v Phipps*, Mr Boardman was ordered to account for all dividends received from his purchase of the impugned shares in breach of duty. Further, the shares were to be held on constructive trust for the trustees (all the trustees). In this sense, equitable remedies are awarded in favour of all beneficiaries — not just those whom are parties to the action. On the facts, Mr Phipps was entitled to a 5/18 share. In principle, all beneficiaries are entitled to their proportionate share and could claim that from Mr Boardman.

A constructive trust should be sought when the plaintiff wants specific control over the assets acquired or produced by the defendant, especially where those assets are likely to further rise in value after the date of judgment.

3 *Restitution of benefit*

(a) Rescission

If the fiduciary wrongly obtains property from the principal, the principal may seek restitution of that benefit by means of equitable rescission. This remedy differs from an account of profits in that the fiduciary need not have made any profit from the wrongful conduct — it simply involves 'handing back' property wrongly obtained by rescinding any relevant agreement by which the wrong was perpetrated.

An order of rescission will normally involve the return of specific, named property to the beneficiary or principal. For example, if property was purchased by the fiduciary from the principal under a contract of sale, that contract will be rescinded and the transaction will be treated as never having occurred.

The status of rescission is unclear. In most circumstances, it is a personal remedy. However, in some cases it appears to have been granted in circumstances closely resembling proprietary characteristics.

(b) Constructive trust

The constructive trust may also be used to effect return of wrongfully transferred property. The fiduciary will be treated as holding that property on constructive trust for the principal. The constructive trust is effectively just a mechanism — a kind of equitable machinery — for returning property to the beneficiary.

For example, in *Chase Manhattan v Israel–British Bank*, the defendant was ordered to hold the overpayment (£2 000 000) on constructive trust for the plaintiff. This was vital because the defendant was insolvent — a constructive trust, being a proprietary remedy, was the only mechanism by which the plaintiff could be assured of the return of their property.

D *Equitable Compensation*

Equitable compensation aims to place the principal in the position in which he or she would have been had the breach not occurred.

1 *History and terminology*

The law of equitable compensation developed in response to perceived inadequacies in common law damages remedies.

Note that it is considered inappropriate to speak in terms of equitable 'damages'. 'Damages' are more commonly relegated to the common law world. Instead, the term 'equitable compensation' is preferred.

2 *Limiting principles*

Equitable compensation differs from common law damages in that it aims to fully replenish a trust after a breach of duty. Notions of foreseeability and remoteness are not used to limit the scope of equitable compensation.

3 *Contributory negligence*

Compensation will never be reduced for the principal's contributory negligence (*Pilmer v Duke*).

***Pilmer v Duke Group Ltd (in liq)* (2001) HCA:**

Issue
- Can contributory negligence affect the relief obtained for brief of fiduciary duty?

Reasoning
- McHugh, Gummow, Hayne and Callinan JJ:
  - There is conceptual difficulty involved in accepting contributory negligence in a fiduciary claim: [86]
  - Contributory negligence focuses on the plaintiff's conduct
  - However, fiduciary law is concerned with the defendant's conduct
  - 'It follows that the allowance by the Full Court of the sum for the issue and allotment of Kia Ora shares, in assessing the damages for breach of contract or negligence, is not to be sustained on the footing that there was a fiduciary duty owed by the appellants, breach of which brought with it a measure of equitable compensation in the same sum'

- Kirby J (dissenting):
  - Equitable remedies serve to compensate and deter; here, clear loss to Kia Ora can be found and should be compensated
  - '**[149]** Where fiduciary obligations exist and have been breached, equitable remedies are available both to uphold the principle of undivided loyalty which equity demands of fiduciaries and to discourage others, human nature being what it is, from falling into similar errors.'
  - '**[150]** The fiduciary must make good any breaches arising from its default in discharging the fiduciary obligations. It must account for any profits it has made

as a consequence. The overall purpose of the law of fiduciary obligations is to restore the beneficiary to the position it would have been in if the fiduciary had complied with its duty.'

- '**[151]** In affording remedies for a fiduciary's breach of its obligations, equity is seen, depending on one's point of view, at its "flexible pragmatic best (or worst)."'
  - 'There are, of course, limits. They are those appropriate to enforcing the obligations of conscience. In a proper case, they will require just counter-entitlements to be set off, or deducted, where this can be done with accuracy. The purpose of equity's relief is not punishment but restoration. The "cardinal principle of equity [is] that the remedy must be fashioned to fit the nature of the case and the particular facts".' (*Warman*)
  - Equity is concerned not only to compensate the plaintiff but to enforce the trust which is at its heart: McLachlin J in *Canson Enterprises Ltd v Boughton & Co*
  - This means that equitable damages will often be greater than common law damages
- If Pilmer had adhered to its obligations, and not acted for Kia Ora in producing the report, 'some other firm of chartered accountants would have been retained who, performing their functions independently and objectively would have been bound on the accepted evidence to report that the price of the shares proposed was *not* a "fair" one within ASX rule 3J(3). Or, in the exigencies, it would have been impossible for the protagonist directors to have obtained a report as required by the rule at all. In either event the requirements for shareholder approval would not have been fulfilled'
- Kia Ora might also have sought informed consent from the shareholders; however, it is 'inconceivable' that the shareholders would have given it
  - Consequently, Kia Ora would not have been able to proceed with the takeover
  - It 'would not have paid the cash and issued the shares'
- The amount of equitable compensation should not be reduced for contributory negligence
  - Likelihood of further impropriety on the part of Kia Ora's directors
    - The Full Court reduced compensation on the basis that Kia Ora's directors probably would have dissipated the company's funds in some other fashion anyway
    - This is not a valid basis for reduction
    - Interest should be awarded for the full term, not just for six months after the takeover, even though this figure is very large as a result
  - Contributing fault
    - There is no authority on whether a concept of reduction for 'contributing fault' can be grafted onto the principles governing equitable remedies
    - '**[170]** Furthermore, all equitable and legal principles must today operate in a universe dominated by the star of statute. It would be surprising if the gravitational pull of statute, felt everywhere else in the law, did not penetrate into the expression and re-expression of non-statutory rules.'
    - Handley: 'Equity has not hitherto considered that a beneficiary is bound to protect himself against his fiduciary. The relationship is not at arm's length and the beneficiary is entitled to place trust and confidence in the fiduciary. The basis for a finding of contributory negligence is therefore lacking.'

Pilmer v Duke makes clear that contributory negligence is not available to shift liability onto the plaintiff in equity. Considerable 'conceptual difficulty' is encountered when trying to import these concepts — especially contributory negligence. Equitable remedies focus on the defendant's conduct whereas contributory negligence is concerned with the plaintiff.

4 *Causation*

There must be some causal relationship between the breach and the loss, unless the action relates to nondisclosure of information. In a case of nondisclosure, the plaintiff–beneficiary need not establish causation to recover. Put more accurately, the defendant will be prevented from pleading a causation argument. That is, a plaintiff will not have to address the argument that they would have lost money even if they had been so informed (eg, in *Hodgkinson v Simms*).

Although causation need not be established in the common law sense, some link must be proven between the defendant's wrong and the loss that is suffered by the plaintiff. A type of 'causation' must be proved (*Youyang*). One formulation is a 'but for' test: that is, but for the defendant's conduct would the plaintiff have suffered loss (*Target Holdings*)? This was cited with approval by the High Court of Australia in *Youyang*, but distinguished on the facts.

***Youyang Pty Ltd v Minter Ellison Morris Fletcher* (2003) HCA:**

<u>Facts</u>

- Youyang Pty Ltd ('YY') is a company that is a trustee of the Bill Haywood discretionary trust (comprising $25 000 000 of investments in total)
- YY invests $500 000 in shares of E C Consolidated Capital Ltd ('ECCCL'), a company carrying on a speculative fund
- A portion of the subscription money paid for the shares is to be used by ECCL to buy a form of security — a bearer deposit — that entitles YY, in ten years' time, to the return of its money as a capital sum
- The remaining money could be used for speculative investments
- Minter Ellison ('Minters') acts as solicitors for the promoters of ECCCL, and agree to hold the money in their trust account as trustee for YY
    - Minters also agrees not to release the funds to ECCCL until they had been provided with a bearer certificate from a prime bank
    - (A bearer certificate is a form of security guaranteeing the bearer repayment of the amount and time described)
    - The share money from YY was to be held in their trust account then released to ECCCL once they had received the bearer deposit so that ECCCL could invest it
- In fact, what happened was this:
    - Minters releases the money to ECCCL without obtaining a proper bearer security
    - All Minters receives is an acknowledgement of receipt (provides no security)
    - Although the receipt documentation is later updated, YY never receives a bearer certificate
    - Four years later, ECCCL becomes insolvent and is wound up
    - No money is available for unsecured creditors
    - However, YY is not a secured creditor because Minter Ellison did not obtain the bearer deposit
- Consequently, YY sues Minters for breach of fiduciary duty
    - YY seeks equitable compensation
    - Hayward claims that he would not have lost the $500 000 but for Minters' breach

of trust

Issue

- Did Minter Ellison breach their fiduciary duty as trustee by releasing the money to ECCCL without obtaining the bearer deposit?
- If so, what should be the remedy to YY?

Reasoning

- Court of Appeal of the Supreme Court of New South Wales:
  - There is a breach of trust
  - However, this breach did not cause the loss to YY
  - This is because supervening events removed the relevance of the bearer deposit
  - YY would have lost the money anyway
  - [See judgment]

- High Court of Australia:
  - There was a breach of duty
    - A conflict of interest also existed (Minters was acting for both the director of ECCCL and YY in the transaction)
    - However, the primary breach was Minters' failure to comply with the terms of the trust on which they held YY's money
    - The terms of that trust required Minters to retain the funds until a bearer certificate was received; in fact, they released the funds without having received such a certificate
  - The supervening events did not break the causal chain
    - YY would not have suffered the loss of their investment but for the breaches of trust by Minter Ellison
  - Distinguishes *Target Holdings*:
    - There the solicitors were in breach by not obtaining the relevant security (a mortgage) before releasing the money
    - However, they did, in that case, at a later date obtain the security
    - It was after this point that the money was lost
    - The solicitors were held not to be liable for the loss because it would have still occurred even had they not breached their original duty
    - It was the fraud of a third party which led to the loss
    - This loss would have occurred anyway
  - Here, however, the loss occurred as a result of the breach
    - A 'but for' test of causation is applied
      - A breach subsequently rectified may negate causation
        - If, as in *Target Holdings*, a non-bearer certificate (providing security) was subsequently obtained to replace the existing bearer certificate of deposit (which provided no security), the effect of Minters' breach would have been ameliorated
        - This 'could be of significance on questions of causation'
        - However, this was not what occurred
      - Dishonesty of third parties is irrelevant
        - 'It is not to the point that, in addition to the breaches of trust by Minters, there may also have been dishonest and discreditable subsequent acts by third parties which led to the loss of the funds'
    - Equitable compensation should be assessed as at the date of judgment, and not the date of breach
      - This contrasts with the usual (though not invariable) rule in tort

and contract that loss is assessed at the date of breach
        - A Court of Equity should use hindsight to determine as accurately as possible the true measure of loss
    - Interest can be awarded on a compound basis to beneficiaries (and not just simple interest)
        - Compound interest will be awarded if the fiduciary was under a duty to invest money, but failed to invest it, or invested it imprudently
        - This amounts to compensation for the profit that would have been made had the money been properly invested
        - The rate at which such interest will be awarded is 'cash rates' (interest which could have been obtained at market rates)
        - Thus, for example, if the investment manager misappropriates funds, the plaintiff will be entitled not simply to the return of the funds, but to their return with interests reflecting the lack of investment that would have been possible had the money been properly dealt with
  - The Court does not expressly disapprove of the *Target Holdings* Court's 'but for' approach
  - Ultimately, however, the test proves difficult to apply in practice

Decision
- The loss is not attributable to other circumstances, so Minters is accountable as fiduciary
- Minter Ellison is liable to pay the total amount of the investment, with interest, from the date it transferred the money to ECCCL through to the date of judgment
- The fact that there were intervening transactions after Minter Ellison's failure to obtain the certificate does not affect their liability because YY's loss could not have occurred 'but for' that failure

Interestingly, Minter Ellison hired rival firm Mallesons Stephen Jaques to defend the claim in the High Court — unsuccessfully, as it turned out.

E *Account of Profits*

In order to obtain this remedy, the defendant must have profited from their breach. If no profit was made, equitable compensation should be sought.

1 *Election of remedy*

If there is a situation where both loss is suffered by the plaintiff *and* a profit made by the defendant, the plaintiff may elect to proceed with either remedy (*Warman International Ltd v Dwyer*). However, that election is binding.

2 *Basis of account of profits*

An account of profits does not depend on whether the principal has suffered a loss or injury. It is not founded in restitution of an unjust gain at the principal's expense. Thus, it does not matter whether the principal was unwilling or unable to make the profit appropriated by the breaching fiduciary.

3 *Extent of profits recoverable*

A fiduciary will be liable to account for profits made within the scope and ambit of his duty.

The profit must also be 'referable' to the breach. This is a kind of causation requirement.

4 *Defences*

An account of profits may be defeated by the following 'defences':

- Estoppel;
- Laches or delay;
- Acquiescence;
- Election (eg, to seek compensation); or
- Where it would be inequitable to assert it.

Whether an account of profits is inequitable depends on the precise circumstances. However, several broad themes may be identified:

- The principal may not stand by and permit the fiduciary to make profits and then claim entitlement to those profits;
- If the profits come from a business acquired or operated by the fiduciary, the principal cannot make the fiduciary account for the whole of the profit of the business
    - A proportion of the profits should be granted
    - The account should be reduced in recognition of:
        - Risks taken by the fiduciary; and
        - The impact of the fiduciary's skill, efforts, property, resources or capital

These defences operate to prevent the remedy being transformed into a vehicle for the unjust enrichment of the principal. The strict rules binding fiduciaries to account for profit should not be carried to extremes (*Warman International v Dwyer*).

5 *Allowance for skill and expertise*

The remedy may further be discounted by an allowance for the fiduciary's skill, expertise and other expenses. The general position is that such an allowance will be made.

***Warman International Ltd v Dwyer* (1995) HCA:**

<u>Facts</u>

- Warman International Ltd ('Warman') carries on a business including acting as distributor (agent) for gearboxes manufactured in Italy by Bonfiglioli
- Dwyer is the Queensland branch manager, an employee of Warman
- In 1986, Bonfiglioli asks Warman to begin assembling the gearboxes in Australia
- Dwyer then tells Warman that he is considering leaving so as to setup his own business (which might include Bonfiglioli)
- In 1988, Dwyer refuses an offer from Warman to purchase the agency division
- Following this, Dwyer incorporates two companies: 'BTA' and 'ETA'
- At this point, Dwyer and Bonfiglioli commence negotiations for a joint venture

- Dwyer enters a distributorship agreement with Bonfiglioli
- Dwyer even arranges to take with him Warman's Queensland staff
- In essence, Dwyer has arranged to take over the Queensland arm of Warman without buying it

- Dwyer resigns; Bonfiglioli terminates its distributorship agreement with Warman
- BTA now takes over distribution of the Bonfiglioli gearboxes
  - Over four years, Dwyer makes $957 000 distributing the gearboxes
  - The loss to Warman represents some $328 000
  - (Warman suffers a small loss relative to Dwyer's larger gain)
- Warman discovers Dwyer's distributive activities, and sues Dwyer, BTA and ETA for an account of profits

<u>Issues</u>

- Is there a breach of fiduciary duty owed by Dwyer as an employee of Warman?
- If there is, what should be the remedy, if any?

<u>Reasoning</u>

- Warman argues that a fiduciary is liable to account for *any* benefit obtained from a breach, even if the principal could not have benefited itself and no loss has been suffered by the principal (strict approach)
  - Thus, there should be an account of profits even if Warman would have lost the agency agreement with Bonfiglioli and discontinued that aspect of its business absent Dwyer's activities

- However, Dwyer contends that Bonfiglioli was going to terminate its agreement with Warman anyway, since the business relationship was not strong (soft approach)
  - Thus, Dwyer should only be accountable for the small amount of profits made until the point at which Bonfiglioli would have terminated anyway

- In response, Warman argues that Dwyer's conduct is dishonest, and that there should be a strict attitude to dishonest conduct by fiduciaries
  - The obligation of a breaching fiduciary to account for the profits of their breach is based on prophylactic (deterrent) and not restitutionary (compensatory) principles
  - Thus, regardless of whether Warman would ever have made those profits itself, the hard approach says that Dwyer's wrongdoing should create an obligation to repay all the money

- In turn, Dwyer argues that equity must be flexible and should not be used in an oppressive way
  - He claims that relief given by equity should be restitutionary
  - Here, he questions: 'what has the plaintiff lost?' given that Warman never fully utilised its business relationship with Bonfiglioli
  - In essence, Dwyer is saying that there should be no account of profits because nothing tangible has been taken from Warman
  - Further, without Dwyer himself, the goodwill remaining in Warman would have been almost nonexistent — Bonfiglioli was displeased with Warman and searching for a new distributor anyway
  - This seems to be based on a causation argument that no account should be made for profits that were going to be lost regardless of the breach

- Trial judge:
  - Dwyer was clearly in breach of his fiduciary duties as employee
  - Dwyer and BTA are equally liable

  - (See below Part III for details of how BTA and ETA, as accessories to the breach, may be held accountable under the rule in *Barnes v Addy*)
  - An account of profits in the amount of $1 000 000 is granted

- Court of Appeal:
  - The decision whether to award equitable compensation or an account of profits is discretionary
  - Here, the lower figure should be awarded: no account of profits will be granted
  - Warman can only recover its loss occasioned from the breach ($328 000)

- High Court of Australia: an account of profits should be awarded, diminished by an allowance for Dwyer's skill and labour
  - Choice of remedy
    - The choice of remedy is a matter for the plaintiff, and not the Court, to decide
      - Eg, if the loss suffered by the plaintiff exceeds the profits made by the fiduciary, the plaintiff may elect to have a compensatory remedy against the fiduciary
    - Once the breach is proved, it is for the plaintiff to choose which remedy will be pursued
      - However, the plaintiff cannot obtain both remedies — the plaintiff must make an election between the two
      - That election is binding upon the plaintiff
      - Otherwise, the plaintiff might be able to make double recovery
    - When must the election be made?
      - The election must be made by the principal once all evidence has been tendered but before the judge hands down judgment

  - Principles governing account of profits
    - The liability to account for profits does not depend on unjust enrichment (ie, does not need to have been made at the principal's expense)
      - Equitable remedies do not depend on whether the principal has suffered a loss or injury
    - It does not matter whether the principal is unwilling or unable to itself make a profit

  - Extent of profits recoverable
    - A fiduciary will be liable to account for profits made within the scope and ambit of his duty
    - The rule that a fiduciary cannot profit from their position is stringent and equity must maintain those high standards (hard approach)
    - The benefit obtained by the breaching fiduciary must be determined as accurately as possible, but mathematical exactness is not required: *My Kinda Town Ltd v Soll* (Slade J)
    - It may be necessary to determine the issue of profits on a voir diré

  - An account of profits may be discretionary, but it still proceeds according to established principles
    - It may, for example, be defeated by the following 'defences':
      - Estoppel;
      - Laches or delay;
      - Acquiescence;

        - Election (to seek compensation);
        - Where it would be unconscionable to assert it; or
            - Eg, the plaintiff may not stand by and permit the defendant to make profits and then claim entitlement to those profits
    - The remedy must be fashioned to suit the nature of the breach and the particular facts
    - Consider:
        - The nature of the property involved in the breach;
        - The relevant powers and obligations of the particular fiduciary involved;
        - Care and skill of the fiduciary; and
        - Tardiness of the principal

- Where a business is acquired and operated, it 'may well be' inequitable and inappropriate to compel the errant fiduciary to account for the whole of the profit of the business
    - Instead, a proportion of the profits should be granted
    - Eg, where a significant proportion of the profits have been generated by the fiduciary's own skill, efforts, property, resources and capital
    - Eg, where the profits have been generated by risks taken by the fiduciary, so long as they are not risks to which the principal's property has been exposed

- The award may be discounted by an allowance for the fiduciary's skill, expertise and other expenses
    - Whether such an allowance will be made is 'a matter of judgment' depending on the facts of a given case
    - In general, however, such an allowance will be made

- The rationale for this limitation is not unjust enrichment but rather the general principle that 'the stringent rule requiring a fiduciary to account for profits can be carried to extremes'
    - That is, where the Court is not concerned with specific assets, the liability of the fiduciary to account 'should not be transformed into a vehicle for the unjust enrichment of the plaintiff'
    - The onus is on the defendant to establish that it would be inequitable to order an account of the entire profits
    - This is so because it is the defendant who bears the risk entailed by mingling profits from a breach with profits earned by their own efforts or investment (similar to a trustee of a mixed fund)

- Application to the case at bar
    - There is a clear breach of fiduciary duty
    - Dwyer must account for the profit made, but only within the scope and ambit of the fiduciary duty
    - Thus, if a profit is made that is outside the scope of the fiduciary duty, no accounting will need to be made for it
    - If Warman's loss exceeds the profit made by Dwyer, it may elect to receive equitable compensation as their remedy
    - Relevance of Warman's failure to notice Dwyer's breach
        - Possibly suggests that it would be inequitable to allow Warman to recover profits which it sat by and allowed Dwyer to make
        - Also suggests that if Warman, as principal, is slow in realising

that the breach has occurred, they would have been unlikely to make any profit by exploiting the business themselves
- Further raises issues of laches

Decision
- Warman is entitled to an account of the net profits after tax made by Dwyer and his companies, commencing on the date on which the joint venture agreement between Dwyer and Bonfiglioli was executed
- However, from the evidence, Bonfiglioli would have terminated the distributorship agreement with Warman anyway — regardless of Dwyer's involvement
  - It would therefore be unfair to award profits indefinitely, or even for four years
  - The award should only cover the first two years of BTA and ETA's operation
- This account must also be reduced by an allowance for the expenses, skill, expertise, efforts, capital and resources contributed by Dwyer
- The case is remitted to the trial judge to determine the amount of interest payable
- Warman should be given additional time (three months) to decide which election to make

Dwyer raises two further issues.

6 *Difficulty of calculating profit*

An account of profits is based on net profit, after tax. However, it can often be very difficult to determine what constitute profit. Expenses are often construed creatively, and are hard to substantiate. It has a deserved reputation as a difficult equitable remedy.

For example, in *Warman*, the remedy is construed as the limited to the profits of BTA and ETA (Dwyer's companies) for the two-year period following their entry into the joint venture with Bonfiglioli. However, supposing Dwyer was paid an exorbitant salary by his companies, this would probably not form part of the net profit over which an account could be sought.

7 *Other deductions*

Where the breach of duty consists of setting up a competing business with the principal, the fiduciary is allowed an equitable allowance for remuneration reflecting his or her contribution to establishing that business.

Thus, in *Warman*, Dwyer was said to be entitled to some equitable allowance (remuneration) for putting his skills, efforts, money, initiative and enterprise to create the secondary business. This would be put into effect as a deduction of the profits required to be disgorged to Warman.

This is similar to *Boardman v Phipps*, in which Mr Boardman was entitled to a generous allowance for remuneration — this was because he 'behaved well', and his breach was 'honest' and 'merely technical'. *Warman* goes beyond this: Dwyer's breach of duty was dishonest, suggesting that remuneration will not be confined to cases in which the fiduciary has acted impeccably.

Perhaps the reason for this allowance relates to the kind of breach and the amount of effort involved in its perpetration. There are, after all, three kinds of breaches:

- Setting up a competing business (*Warman*, a distributorship);
- Taking property (*Chan v Zacharia*, a lease); and

- Purely technical breaches (*Boardman v Phipps*, management of shares).

In general, courts seem to be saying that fiduciaries in the second class (property) will not receive an allowance, whereas fiduciaries in the first class will. *Boardman* probably represents a class in which the fiduciary is morally blameless.

These distinctions probably stem from equitable concerns for 'sweat of the brow': the fiduciary who has invested time and effort in a productive enterprise (competing or not) deserves some recognition for that effort. The Court seems to be saying that whether an allowance is granted will be determined by the quantum of the fiduciary's effort, which must be beyond some minimum threshold of productivity; that is, it must achieves a substantive result. However, a passive breach, such as misappropriation of property, involves little effort and deserves no compensation.

F *Rescission*

Where the creation of a contract itself constitutes a breach of fiduciary duty, a court of equity can order its rescission as a remedy for that breach of duty. For example, if a fiduciary profits from a purchase from his principal, or a fiduciary fails to disclose her interest in a loan secured against property owned by her principal, the contract of sale, and the contract of loan may be rescinded, respectively (*Maguire v Makaronis*).

The failure of a fiduciary to disclose their interest in a transaction resulting in the assumption of contractual obligations is 'material'. This means that the Court cannot postulate what the principal would have done had the fiduciary disclosed their interest — the situations are inherently incomparable. Thus, a causation argument, to the effect that the principal would have proceeded with the loan or purchase even if they knew it was from the fiduciary, must fail (*Brickenden v London Loan & Savings Co*).

Brickenden v London Loan & Savings Co **[1934] Privy Council:**

<u>Facts</u>

- Brickenden is a solicitor who acts for a finance company, London Loan & Savings Co ('LLSC')
- LLSC seeks to make a loan to one of its clients, a Mr Biggs
- Brickenden organises the loan to Biggs in such a way that he receives certain fees and commissions
- Brickenden does fails to receive the informed consent of LLSC to these payments
- LLSC subsequently seeks to escape the loan and argues that it should be set aside as a breach of fiduciary duty by Brickenden
- Brickenden argues that, even if LLSC had been informed of the payments, they would have proceeded with the loan anyway

<u>Issue</u>

- Can the loan agreement be rescinded by the Court as a remedy for breach of fiduciary duty?

<u>Reasoning</u>

- Brickenden is liable to the client for the loan and interest, less certain deductions
- This is so notwithstanding that LLSC probably would have proceeded with the loan even had its source been disclosed
- Brickenden solicitor cannot rely on this causation argument because (at 469), where the

non-disclosure is 'material', the counter-factual cannot be postulated:
    - Brickenden could not 'be heard to maintain that disclosure would not have altered the decision to proceed with the transaction, because the [company's] action would be solely determined by some other factor, such as the valuation by another party of the property proposed to be mortgaged. Once the Court has determined that the non-disclosed facts were material, speculation as to what course the [company], on disclosure, would have taken is not relevant.'

<u>Decision</u>
- An 'equity for rescission' arises by virtue of the breach of fiduciary duty
- LLSC can exercise the equity and rescind the loan

Brickenden has since been accepted in Australia by the High Court of Australia's decision in *Maguire v Makaronis*.

In that case, a majority of the Court held that a breach of duty occasioning the creation of a contract 'immediately' gives rise to an equity of rescission in the wronged principal entitling them to rescind that agreement. Although Kirby J agreed on the outcome, his Honour added a further requirement, applying *Brickenden*, that the breach — typically non-disclosure of an interest in the transaction — be 'material'.

Maguire v Makaronis **(1997) HCA:**

<u>Facts</u>
- Maguire acts as solicitor for Mr and Mrs Makaronis in the purchase of a poultry farm business and attendant property
- In order to finance the purchase, the Makaronis obtain a loan of $250 000 from Maguire
- This loan is secured by way of mortgage over another property owned by the Makaronis
- However, Maguire does not disclose that he will be mortgagee of the loan
- The Makaronis cannot afford to repay the loan, making only one repayment
- Maguire commences an action for possession of the farm property
- However, the Makaronis issue a counter-claim, seeking to have the mortgage set aside as a breach of fiduciary duty
- In response, Maguire argues in reliance on an old Canadian authority (*Brickenden v London Loan & Savings Co*) that the Makaronis would have gone ahead with the purchase and mortgage even had they known of and given consent to the breach

<u>Issue</u>
- Can the agreement of mortgage be rescinded by the Court as a remedy for breach of fiduciary duty?

<u>Reasoning</u>
- Brennan CJ, Gaudron, McHugh and Gummow JJ:
    - A breach of fiduciary duty clearly occurred here
    - The duty was that owed by a solicitor to their client (presumed category)
    - The nature of the breach was a reasonable possibility of conflict between his duties to the Makaronis as clients and his own personal interest in the transaction
    - The Makaronis had not consented to the breach
    - The mortgage is set aside, on one condition: the Makaronis must still repay the money borrowed

    - An equity of rescission arises from the appellants' breach of fiduciary duty
        - This (mere) equity (a kind of personal, equitable right) entitles the borrowers to set aside the entire transaction — to rescind it — so as to return the parties to their original position
        - Rescission *restitutio in integrum* is possible, unlike *Vadasz v Pioneer Concrete (SA) Pty Ltd*, because the agreement can here be completely (and not merely partially) set aside

- Kirby J:
    - *Brickenden* should be applied
        - A purely 'causative approach' to breach of duty would make it difficult to attribute responsibility to breaching fiduciaries, especially where multiple intervening causes are present
        - Such an approach could also be seen to sanction the breach where new causes intervened, by providing no relief to the beneficiary
        - By contrast, *Brickenden* bears an attractive simplicity; it is certain
        - The *Brickenden* rule also has desirable prophylactic consequences; it helps ensure the strict loyalty and good faith of fiduciaries, deterring them from abusing their powers
    - The non-disclosed interest of Maguire in the mortgage was material
    - All the subsequent events hinged upon that non-disclosure: they would not have occurred but for the breach
    - The breach resulted in the execution of a flawed mortgage instrument
    - Possible orders are flexible and broad; they must be fashioned to the particular facts:
        - Order of rescission
        - Finding of a constructive trust
        - Application of tracing principles
        - Imposition of an account of profits
        - Award of equitable compensation (especially where rescission is impossible)
        - Injunctive relief, *et cetera*
    - Apportionment may prevent a fiduciary being burdened with the consequences of a beneficiary's own unreasonable conduct, but it — like contributory negligence (and see now *Pilmer v Duke* per Kirby J) — has been the subject of criticism

<u>Decision</u>

- The mortgage is set aside for breach of duty
- However, the Makaronis must first repay the money borrowed

In practical terms, the Court's remedy seems a relatively futile attempt to compensate the respondent purchasers. Given their impecuniosity, the only way they could have satisfied the Court's conditional order would be to sell their farm as if the appellants' repossession action had been successful. Alternatively, they could have obtained a bridging loan, but this would likely have been on similarly unworkable terms. Thus, although the Court's order nullified the breach in *form*, the effect was much the same as if the loan was still in force.

G *Constructive Trust*

1 *Characteristics and effect*

A constructive trust is a remedial order vesting an equitable right to property in the claimant. The unsuccessful defendant against whom a constructive trust is ordered is deemed to hold the subject property on trust for the claimant.

It follows that the imposition of a constructive trust results in two consequences. First, a proprietary interest in the asset is given to the plaintiff. This means that the plaintiff will have priority over unsecured creditors in the event of the trustee's bankruptcy. Second, the plaintiff will have ownership of all future profits produced by the asset. The remedy is effectively a perpetual account of profits, as well as control over the future management of the asset.

Because of these consequences, the constructive trust is a highly sought after remedy.

2 *Requirements*

There must be a connection between the breach of duty and the property being claimed. That is, the property which is to be the subject of a constructive trust must be 'referable' to the breach. A plaintiff will not simply be entitled to any property owned by the fiduciary by virtue of that fiduciary's breach.

For example, where a fiduciary steals a car from his principal, a constructive trust may be awarded over the car. In more complex cases, as where the fiduciary's breach lies in setting up a competing business or receiving an unauthorised gift of land, the relevant asset may be the business itself, or the land, respectively.

3 *Examples of imposition*

In *Boardman v Phipps*, a full account of profits was granted, but the Court did not differentiate between that remedy and the constructive trust because their effects were on those facts the same.

In *Hospital Products*, the Court of Appeal of the Supreme Court of New South Wales was willing to award a constructive trust over all of HPL's assets. This would have meant that USSC could close down or continue to run Hospital Products Limited. This would have been an example of the constructive trust being used for profit disgorgement — the business comprising the breach would have been vested in the plaintiff. *LAC v Corona* is also an example of this.

In the High Court of Australia, Mason J was prepared only to give a limited constructive trust. It was not over all the assets of HPL and HPI, but instead restricted to the profits made between the period of HPI's commencement of operation and transfer of assets to HPL. It was further discounted in two respects.

First, an allowance was to be made for HPI's work and skill. Second, the nature of the breach suggested that HPI was not permitted to compete in Australia with USSC, but nothing prevented it to competing with USSC in the United States. If a full constructive trust were granted, this would have gone beyond what was appropriate — it would prevent HPI from ever competing with USSC anywhere, even though that would not have been a breach. The remedy was therefore narrowed to the scope of the actual breach. Effectively, what was granted was an account of profits secured by equitable lien over the business' assets.

4 *Moment of creation*

A constructive trust will ordinarily arise at the time of the Court's declaration (ie, the moment of judgment) since it is traditionally viewed as a remedial device. However, there is considerable flexibility concerning the terms of an order of constructive trust.

For example, the Court retains discretion to backdate the trust's creation to a more appropriate time. In this way, the Court can ensure its order is complied with despite the existence of a prior equitable interest in a third party, which would normally render illusory the relief granted by way of constructive trust.

5 *Transfer of assets*

A constructive trust will not be granted over property that has already been transferred to a *bona fide* purchaser for value without notice. (Even if a court did make such an order, the purchaser's influence would ultimately prevail in an equitable priority contest.)

If, for example, in *LAC Minerals v Corona*, LAC had already sold the mine to a third party before the Canadian Supreme Court handed down judgment, the Court could not have made an award of constructive trust in favour of Corona. Of course, this assumes that the hypothetical transferee was not actually or constructively aware of the litigation and impending judgment, and proceeded in good faith rather than as an accomplice to fraud.

H *Bribery Cases*

A bribe is a gift accepted by a fiduciary as an inducement to him to betray his trust. When a bribe is received by a fiduciary in the course of her duties, it is a breach of duty for which account must be made to her principal.

At a minimum, the fiduciary will have to pay equitable compensation to the principal, or to account for the proceeds of the bribe. However, the fiduciary may also seek a constructive trust over any assets acquired with the bribe, or, where the bribe is itself the gift of certain assets, the assets themselves. However, property traceable to the receipt of a bribe presents certain issues that may affect the grant of a constructive trust over that property.

Issue: can the principal recover from the fiduciary the proceeds of the bribe? Specifically, will a court of equity grant a constructive over those proceeds, despite them being wrongfully obtained?

The traditional view is strict and unsympathetic to the principal: a constructive trust is simply unavailable where the assets over which it is sought were procured by a bribe (*Lister & Co v Stubbs*). This position reflects equity's dim view of parties who seek to profit from the dishonest conduct of another, especially where this would come at the expense of other, more deserving parties (such as unsecured third party creditors).

Lister & Co v Stubbs (1890) UK Ch:

Facts

- The plaintiff carries on a business as a silk dyer and manufacturer
- The defendant is a foreman formerly employed by the plaintiff
- One of the defendant's duties is to purchase materials from suppliers

- The defendant takes large bribes from one such supplier in return for preferential treatment by the silk business
- With this money, the defendant makes various investments
- The plaintiff discovers the bribery, and seeks a constructive trust over those investments

<u>Issue</u>

- Should a constructive trust be imposed in favour of the plaintiff?

<u>Reasoning</u>

- There is a clear breach of fiduciary duty by the defendant, in taking the bribes
- Although there is a breach of duty, the remedy of constructive trust is not available
    - The relationship between employee and employer here is one of debtor–creditor only (not trustee–beneficiary)
    - It is a personal, common law relationship — not one where the defendant holds property for or on behalf of the plaintiff (an equitable property relationship)
    - All that can be said is that the defendant owes a personal obligation to repay his employer the bribes

- Lindley LJ: there would be 'startling consequences' from the award of a constructive trust in these circumstances
    - The plaintiff would receive priority over the defendant's other creditors
    - Any profit made from the investments would also go to the plaintiff
        - This is 'inappropriate' having regard to the fact that the assets are the result of a bribe
    - Consequently, the obligation is a personal debt only — not a constructive trust
        - [Arguably, this does not sit well with the deterrent objectives of equity (*Boardman v Phipps* — even an innocent breach)]
        - [Here, if even a dishonest breach is incapable of providing a proprietary remedy, this diminishes the deterrent effect of fiduciary law]
        - [Why are these consequences so startling when they are the ordinary consequences of imposing a constructive trust?]

<u>Decision</u>

- The employer is limited to personal remedies against the breaching fiduciary
- It would be inappropriate to impose a constructive trust over the investments when this would deprive the defendant's other creditors of their interests in the property

Some commentators have described *Lister* as an anomaly and bad law. Indeed, and with respect, it seems difficult to extract any sound statement of policy from the judgment of Lindley LJ. Nevertheless, because of *dicta* appearing to approve *Lister* in Australia, it remains relevant.

In the United States of America, *Lister* was conclusively rejected: bribe property is there held on constructive trust for the principal.

Many restitution scholars have argued that *Lister* was in fact correct: if there was no unjust enrichment at the expense of the plaintiff, no constructive trust should be available. In *Lister*, the property never belonged to the plaintiff — it was third party property in which the plaintiff had no proprietary rights. The enrichment was at the expense of the person from whom the bribe was originally taken — not the principal. However, it may also be argued that the plaintiff was disadvantaged by the breach (for example, by receiving poorer quality or more expensive components). This would mean that the fiduciary's enrichment was at least partially at the expense of his principal.

Further, this restitutionary approach undermines the deterrent aspect of fiduciary remedies. Given that accepting a bribe is one of the worst breaches that can be committed — even when it does not affect the principal — surely the most powerful proprietary remedy should be available. See, eg, the comments made in *Boardman v Phipps* and *Maguire v Makaronis* about the prophylactic role of equitable remedies.

More recently, in *Attorney–General for Hong Kong v Reid* (‘*Reid*’), the House of Lords articulated a rather different approach to the scenario in which a fiduciary entertains bribery. *Reid* represents a significant departure from *Lister*, permitting a constructive trust to be imposed over all property the subject of the bribe without discrimination as to its means of procurement.

However, because *Reid* has not, to the author’s knowledge, yet arisen for consideration in Australia, it is unclear which approach would be preferred as a matter of law. Consequently, when considering a case involving bribery, it will be necessary to consider both approaches and make an argument as to which would produce the preferable result.

***Attorney–General for Hong Kong v Reid* (1994) HL:**

<u>Facts</u>

- Reid, a New Zealander, works in Hong Kong
- He rises to the position of acting director of public prosecutions
- As an employee of the Crown, he owes it fiduciary duties
- He breaches this duty by accepting bribes to drop charges against certain individuals
- He is sentenced to eight years’ imprisonment
- He is also ordered to pay $12.4m to the Hong Kong employer (the value of assets derived from the bribes)
- Some of these assets include property that he has purchased in New Zealand
- The Hong Kong government argues that it is entitled to a constructive trust over those properties
- This decision concerns an application by Reid to determine whether caveats on those New Zealand properties should be removed
- If a constructive trust is potentially available, no further dealings should be permitted with the property, and the caveats should remain in place

<u>Issue</u>

- Is a constructive trust the appropriate remedy?
- If so, can the caveats be removed from the register of titles?

<u>Reasoning</u> (Lord Templeman)

- Status of the authorities
    - The New Zealand court views itself as bound by *Lister*, holding that no constructive trust exists and removing the caveats
    - However, on appeal to the Privy Council, it holds that New Zealand courts are not bound by *Lister*, and, further, that on principle a constructive trust should be imposed

- Equitable and legal title
    - When a bribe is received by a fiduciary (‘the false fiduciary’), it belongs in law to that recipient
    - Similarly, any freehold property conveyed to the false fiduciary by way of bribe vests in him
    - ‘Equity, however, which acts *in personam*, insists that it is unconscionable for a

fiduciary to obtain and retain a benefit in breach of duty'
  - The provider of the bribe cannot be granted its recovery, since making it was a criminal offence
  - Instead, the false fiduciary must account for the bribe to his or her principal

- Accepting a bribe is a clear breach of duty by the employee
  - It is an 'evil practice'
  - In law, the bribe profit belongs to the breaching fiduciary
  - In equity, however, the bribe belongs to the principal (the Hong Kong government)

- It would be unconscionable for a fiduciary to retain a benefit obtained in breach of duty
  - The fiduciary became a debtor in equity to the principal for the amount of the bribe
  - If, however, the bribe consists of property which rises in value after its receipt, or cash that is invested advantageously, the false fiduciary must be accountable not only for the bribe but also for the additional proceeds
  - Otherwise, the fiduciary would be permitted to retain a benefit
  - The bribe should have been transferred instanter to the principal
  - Since equity regards as done that which ought to have been done, the bribe is deemed transferred to that principal
  - Consequently, as soon as a bribe is received — whether in cash or in kind — the false fiduciary holds it on constructive trust for their principal

- 'We are not concerned with the objections raised to the granting of a constructive trust in this context'
  - Two objections are traditionally raised:
    - A fiduciary cannot be both debtor and trustee
    - The unsecured creditors of the fiduciary would be deprived of their share in the bribe property
  - These objections are not insurmountable:
    - The two remedies (account of profits and constructive trust) can exist simultaneously in the alternative, providing there is no double recovery
    - Other creditors cannot be in a better position than the fiduciary
    - Since Reid doesn't own the properties, how can his creditors make any claim to them themselves?

- They properties are therefore owned by the Hong Kong government in equity
  - Any other result is inconsistent with the fiduciary principle: *Keech v Sandford*; *Boardman v Phipps*
  - The strict approach should be adopted: if gains by innocent fiduciaries can be held on constructive trust, surely gains made by criminal fiduciaries can be so held

<u>Decision</u>

- A constructive trust is imposed over the investment property and bribe proceeds
- Overrules *Lister* (though *Lister* may still be relevant in Australia)

As a result of *Reid*, the controversial decision in *Lister v Stubbs* has been overruled in England (and the then British-controlled dominion of Hong Kong). Its status in Australia remains unclear, despite favourable comments in *Zobory v Commissioner of Taxation*, with the matter yet to come before any appellate court for decision. Nevertheless, according to Meagher, Gummow and Lehane, '[i]t seems likely that *Reid*'s case will be followed in Australia.'

IV *Hypotheticals*

A *Hypothetical Taxonomy*

Economic interests: start with the existence of a relevant relationship —

1 *Is there a fiduciary relationship?*

- *Hospital Products* (Mason J): undertaking
- *Hospital Products* (Dawson J): vulnerability
- *UDC v Bryan*: mutual trust and confidence (horizontal cases)
- *Smith*: 'reasonable expectations', reliance

Eg, joint venture: mutual trust primarily relevant (since horizontal). But also mention overlapping tests.

2 *Has the fiduciary relationship been breached?*

(a) What are the obligations?

(i) No unauthorised profit
(ii) No conflict or possibility

(b) What are their scope and ambit?

(i) Depends on the relationship
(ii) Not all wrongful conduct constitutes a breach; eg, negligent conduct won't amount to breach of duty
(iii) Discuss *Breen v Williams*
(iv) *Hospital Products* (Mason J)

(c) Do the acts complained of constitute a breach?

(i) Conflict of interest: real and sensible possibility (*Chan*)
(ii) Unauthorised profit (*Boardman*)
(iii) Failure to comply with terms of trust (*Minter Ellison*)
(iv) Breach of confidence (*LAC Minerals*) and other imprudent conduct

3 *Defences*

(a) Did the beneficiary give fully informed consent to the conduct comprising the alleged breach?

(i) Complete defence
(ii) Must be fully informed
(iii) Some parties incapable of giving fully informed consent (*Boardman*)

(b) Did the plaintiff unreasonably delay the proceeding?

4 *What is the appropriate remedy?* ***[Generally most important]***

(a) Compensation

(i) Is the loss greater than the profit?

(b) Account of profits

(i) Over what period?

(c) Constructive trust

(i) What is the subject property? Identify precisely
(ii) Scope?

(d) Liens

(e) Bribery

(i) Is the subject matter of the breach the receipt of a bribe?

(f) Third parties

(g) Tracing

Non-financial interests: start with a consideration of whether there is any relevant interest —

1 *Proscriptive approach* (don't mention in pure economic interest case)

(a) Subject matter of the breach

(i) Where is the profit?
(ii) Where it the conflict?
(iii) If no relevant subject matter, Court may not even ask whether a fiduciary relationship exists

(b) Subject matter of the duty

(i) Positive?
(ii) Negative?

(c) Analogy with settled principles

(i) Essential elements of fiduciary relationship
(ii) Undertaking test
(iii) *Et cetera*

2 *Breach*

(a) Scope of the duty
(b) Alleged breaches
(c) *Et cetera*

B *Hypothetical 1*

1 *Introduction*

- Trico Ltd (‘T’) has suffered pecuniary loss, financial profit
- T can allege breach of duty against Angela (‘A’) and claim an equitable remedy
- A’s alleged breach involves profiting from her position as T’s marketing consultant and pursuing a conflicting commercial interest in Angietoys (‘AT’)
- This scenario falls well within the boundaries of the proscriptive approach, so a traditional structure will be adopted
    - First, examine whether a fiduciary relationship exists between A and T
    - Second, then consider whether A has breached it
    - Third, consider which remedies will be available against A and AT and the extent to which T will be able to recover its $4m loss

2 *Is the relationship of a fiduciary character?*

- Employee–employer
    - The employee–employee relationship is a presumptive category of fiduciary duty
    - Although A was once an employee, that relationship ceased when she left T
    - It is unclear whether she is now an employee or an independent contractor (is her current position one of employee?)
    - Continuing obligations — *Chan v Zacharia* (continuing obligations between ex-partners, until full winding up of partnership) — confidential information whilst an employee
    - However, even if she is a contractor, the relevant tests are probably satisfied on the facts (see below)
    - Alternatively, it might be argued that A is T’s agent (presumptive category)

- *Hospital Products* (Mason J): undertaking
    - Consultant–client is not an established fiduciary relationship
    - Although A may be retained under a research contract, fiduciary obligations can coexist alongside contractual and tortious ones, such as A’s duty to exercise due care and skill
    - A undertook to act on T’s behalf to investigate gaps in the toy market and propose a profitable product for T to develop
    - An undertaking in the exercise of a discretion capable of affecting the principal’s interests;
    - In this capacity, A represented T as their marketing consultant
    - Discretion: she first carried out consulting work on her behalf
    - Effect on interests: she then proceeded to oversee the complete development of the product (business success a relevant interest), entering into legal relations on T’s behalf (legal interests)
    - There is a clear undertaking to research and manufacture a toy for T that would meet T’s interests by being profitable
    - Had the toy been manufactured, A might well have been made its distributor, as Blackman was in *Hospital Products*
    - Both undertakings occurred in circumstances where the fiduciary had a ‘special opportunity’ to cause harm to the principal
    - Here, A could (and did) use the market research for her own ends

- *Hospital Products* (Dawson J): vulnerability (also relevant)

  - Consultant–client is a vertical relationship: the client reposes confidence in the consultant to carry out independent analysis
  - Here, A was one of T's 'trusted' employees, and A clearly placed trust in A's ability and honesty
  - T was in a position of vulnerability in three respects:
    - It placed absolute faith in A's abilities and honesty (like *CBA v Smith*)
    - It was in an insecure financial position
    - It entrusted A with confidential information about its strengths, weaknesses, and gaps in the market
    - It relied on the success of her plan to regain profitability
  - But was it simply an arms length commercial transaction? But should T have protected itself?
    - Apparent lack of contractual safeguards to regulate their relationship — why should fiduciary law fill the gaps? (weak argument)
    - However, may itself evidence trust and vulnerability, like the unsecured payment of money in *UDC v Bryan*

- *Smith*: 'reasonable expectations', reliance
  - The situation is a little similar to *Smith*, albeit involving a consultant rather than a financial adviser
  - A has a long history with T — it was not an arms length commercial transaction
  - T did not obtain independent advice, and trusted A absolutely
  - T reasonably expected A to act in its interests
  - T's failure to protect itself was reasonable:
    - Examine industry practice (*LAC Minerals*) — consultants generally entrusted with responsibilities and confidential information without formalities

- Conclusion: whether on the undertaking, vulnerability or expectations approaches, a fiduciary relationship exists

3 *Has the fiduciary relationship been breached?*

(a) What are the obligations?

(i) No unauthorised profit (*Chan v Zacharia*)
(ii) No conflict or possibility (*Boardman v Phipps*)

(b) What are their scope and ambit?

- Scope of the relationship
  - In the circumstances, it appears that the consultant–client relationship exhibits fiduciary characteristics (undertaking, vulnerability)
  - Initially, A's only task is to design a suitable toy (not especially fiduciary)
  - Later, in paragraph two, A is tasked with implementing the plan to manufacture

- What, then, is the scope of that relationship?
  - A was not to make business decisions by reference to her own interests: her task was purely to assist T in recapturing the toy market
  - She was also positively obliged to oversee the development of the toy
  - A was also obliged not to act in a way that created a 'real sensible possibility of conflict' between her interests and those of T
  - Thus, like Blackman in *Hospital Products*, A was obliged not to compete with T in the toy market or to injure its new product

  - This would create actual conflict between their interests, since the products would be in direct competition

- It seems clear that the relationship extended to not developing a competing toy and not misusing the information about T's new toy or poor financial position for her own purposes

(c) Do the acts complained of constitute a breach?

- A breached her fiduciary duty to T by engaging in conduct during the period of consultation with a view to appropriating T's market for herself
- Specifically, A:
  - Deceived and competed with T
    - She secretly developed a capacity to manufacture the toys she was meant to be implementing for T
    - She stopped implementing the rollout of T's plan in favour of these secret activities
    - She deceived T about the status of the project and concealed her plans from T, all the while laying the foundations for her own commercial enterprise
    - She sold the competing toys under her own name without T's informed consent
  - Receipt of bribe
    - She accepted $100 000 in return for preferential treatment with T
  - Breach of confidence [**mention**]
    - Unauthorised use of confidential information belonging to T, which is confidential
    - Information: plans for toy, market data, T's strengths and weaknesses
    - Did the information belong to T or to A? A will argue that since she developed the toy it was hers
    - However, prima facie it was T's since the information was created during the term of the agency/employment (*LAC Minerals*)
- Bribe:
  - Clearly within scope and ambit of duty (through her work as agent/consultant)
  - Clear conflict (quality of paint versus personal financial interest)
  - Clear profit and benefit from her position as fiduciary
- Competition:
  - A's very job was to develop a new toy on T's behalf; she did that on her own behalf
  - Therefore within the scope of the duty
  - In doing so, A obtained a significant windfall ($2m), in breach of the 'no profit' rule (*Chan v Zacharia*), which is enforced strictly (*Boardman v Phipps*), especially where — as here — the breach occurred in bad faith
  - She profited from her position: knowledge of the gaps in the market obtained through her fiduciary role
  - Also a substantial conflict: in direct competition with her principal (*Pilmer*): duty (to develop *successful* toy), self-interest (developing her own *successful* toy), where success of one can possibly reduce the success of the other
- All of this happened without T's informed consent (the truth was actively concealed from them by A)

4 *Are any defences available?*

- No informed consent given (indeed, truth actively concealed)
- Laches (delay) — weak
    - No fixed period
    - Here, two years after breach, one year after discovery
    - Mitigating circumstances
    - Impossible to determine whether it would be barred
    - Arguably not undue delay: T still permitted to sue
    - However, might still affect the remedy granted

5 *What is the appropriate remedy?*

(a) Breach 1: bribe

- A seeks a constructive trust over AT's profits
- It is arguable that at least some of these profits were procured by a bribe, in that $100 000 of her startup capital came from a payment by a paint manufacturer in return for preferential treatment by T
- Is T prevented from obtaining a constructive trust over these profits?
- *Lister* approach: no constructive trust since this would lead to priority anomalies
    - Like *Lister*, taking this bribe was a clear breach of duty
    - Like *Lister*, the relationship did not involve holding property
    - Here there is no risk that AT's unsecured creditors will lose priority to a constructive trust occasioned by bribe, since the only other interest is held by the bank as a registered mortgage (a prior legal right already having priority)
    - There are thus no 'startling consequences' (Lindley LJ)
- *Reid* approach more applicable:
    - It would clearly be unconscionable for A or AT to retain the extensions as benefits of her breach of duty (accepting the bribe)
    - Necessary to deter persons in A's position from bribery, especially where A has since dissipated the received assets into other property
    - Gains of criminal fiduciaries should be held on trust
- *Reid* probably good law, but unclear
    - If it is applied, a constructive trust would be imposed over the property into which the bribery funds were invested (the extension to A's home)
    - But: what is the nature of the extension?
        - If it is a discrete unit, it might be easily separated and made the subject of a constructive trust
        - However, if it cannot easily be distinguished from the main property, a problem might arise
        - It would be difficult to identify precisely the subject matter of the property
        - The remedy needs precisely identifiable property to be imposed
    - Look for doubt in the subject matter property

(b) Breach 1: alternative remedies

- Equitable compensation
    - What is the loss?
    - Difficult to assess the impact of the bribe on T (reduced service levels, more expensive, etc)
- Account of the profits of the bribe ($100 000)
    - Could secure by equitable lien (as in *Hospital Products* NSW CA, reversed on other grounds by HCA) to survive insolvency

(c) Breach 2: compensation

- A estimates the 'loss' at $4m
  - Can the lost opportunity to make income amount to a loss?
    - Yes, expectation loss
    - Loss of market share
    - Loss of expected profits
    - *LAC Minerals*: apparently so
  - Reduction might be made for A's expenditure, taking the risk of the loan and investing in the plan
  - However, T was willing to take that risk anyway — indeed, was asking A to help it take that very risk in developing the toy
- Because T's loss is greater than the profit made by A and AT, equitable compensation may be the most appropriate remedy
- Causation issue: but for A's breach of duty, it seems likely that T would have gone on to successfully implement the plan to sell the toy (*Youyang*)
  - This is evidenced by the fact that A, undertaking similar preparations, was able to reap such a significant profit
- However, this is a personal remedy enforceable only against A, not AT
  - Unless AT is gone after as an accessory
- Since A conveyed her home to AT, A probably has insufficient assets to make good on the order for compensation
- No reduction for T's possible contributory negligence in failing to protect itself by contractual means or monitor A's progress (*Pilmer v Duke*)
- But reduction for failure to mitigate (*Smith*)
- There is some risk of A obtaining a net benefit from the breach, for example in the extension to her home, and subsequent gains from the manufacturing machinery
- AT effectively has a platform — through the machinery — to continue competing with T, so the breach would be continuing even after the payment of compensation
- Paying compensation may thus be insufficient deterrent against wrongful conduct
- Question whether T would have actually earned $4m itself
  - Lack of inertia
  - Lack of awareness of the market
  - Financial vulnerability
  - Did have retail contacts, though
  - But T shouldn't be able to watch AT profit, then claim the profits

(d) Breach 2: account of profits

- An account of profits would entitle A to recover the $2m made by AT as a result of A's breach of duty, and any interest or other secondary income obtained thereby
  - T must elect which remedy it wishes to pursue (*Warman*)
- Equitable compensation would entitle it to greater recovery, but it is unlikely to obtain the full amount either way
- If an election is made for the account of profits, there may be a reduction for skill and labour ($200 000 expenditure) — an allowance for A's work (also for compensation)
  - Should A be entitled to an allowance?
  - *Boardman v Phipps*: only honest fiduciaries
  - A is not honest (bribing, deceptive)
  - *Warman*: dishonest fiduciaries still may be entitled to an equitable allowance
- Delay argument also applies

(e) Constructive trust

- As an alternative to an account of profits, T could also seek a constructive trust over:
    - A's assets (equipment, money in bank accounts)
        - (Note briefly priority issue against bank loan)
    - AT and its assets (including accrued profit, with interest), including machinery and existing stock
    - **Not** 'over AT' or 'over A' (must be specific assets)
- Ie, T must elect for an account of profits, and the Court must decide that the assets are part of the profit
    - Ie:
        - Breach of duty
            - Profit
                - Account of profits (personal)
                - Constructive trust over profits (proprietary)
                - The choice is not by election but determined in the Court's discretion
            - Loss
                - Equitable compensation (personal)
- This could be useful for T if AT was doing well and T wanted to continue using A's existing equipment to immediately recommence production and sales using its retail contacts
    - Or it could close down the business completely
- *Warman v Dwyer*: onus rests on defendant to show why a constructive trust should be imposed over a whole business (rather than property)
    - Contribution of Angela's own care and skill in building the business: may reduce the extent of the profits, or grant an allowance, or deny a constructive trust
    - However: that care and skill was the every reason for being approached by T — they are fully within the ambit of her obligations, so this excuse may not be effective (unlike Warman's skills in *Warman v Dwyer*)
    - Unlike *LAC Minerals*, the extent of the profit is relatively certain: an injunction can be granted to restrain further manufacturing or sale of the competing toy
    - Are the valuation techniques inaccurate? (Wilson and La Forest JJ)
    - However, constructive trust would prevent A and AT from profiting in any way from A's breach:
        - T would gain title in A's assets, including machinery and what was once A's house
        - Is this too much? Should T gain A's house? Arguably overcompensates — goes beyond corrective justice between the parties, essentially since T might still go on to sell the toys successfully itself, thus mitigating its anticipated losses
- Laches
    - Equity aids the prudent not the tardy — might be used to resist imposition of a constructive trust or reduce account of profits
        - T delayed bringing the action for a whole year after it discovered the breach
        - Financial hardship may be a mitigating factor here, though
    - It may also demonstrate that such hardship and ineffectiveness may have prevented it from pursuing the plan effectively on its own, thereby reducing the extent of liability — took them a year to realise the toy was on the market
        - But it did have strong a retail network
        - Based on unjust enrichment, though — arguably not relevant to an account of profits (which are to be completely disgorged), but may limit the period during which profits must be accounted: ie, <$2m

(f) Liens

- If a constructive trust is unavailable, an account of profits could be secured by an equitable lien enforceable against AT
- *Hospital Products*

(g) Accessories

- Note that the Bank could potentially be liable as an accessory to the breach (by providing the loan)
- AT: knowing receipt of breach of trust property (*Barnes v Addy*)

(h) Third parties

- If the bank loan is a registered mortgage, it will have a prior legal interest that will have to be satisfied first if AT enters liquidation, potentially reducing T's enforceable award
- Rescission would be available to T against the paint manufacturer (*Makronis v Maguire*)

C *Hypothetical 2*