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Fiduciary Duties

What is a fiduciary relationship?
A fiduciary relationship arises under common law where A and B agree that A will act on behalf of or for the benefit of B in circumstances which give rise to a relationship of trust and confidence. A has some discretion or power which affects B's interests. B in turn relies on A for information or advice. In determining whether a relationship is fiduciary, the substance of the relationship must be examined in light of its commercial context and the entirety of the obligations undertaken (and not just the label given to the relationship).

Fiduciary duties are owed by:

- Partners (to their fellow partners).
- Solicitors and other professional advisers (to their clients).
- Trustees (to beneficiaries).
- Agents (to principals).

Directors
Under equity, directors have owed fiduciary duties to their companies. Chapter 2 of Part 10 of the *Companies Act 2006* (CA 2006) codifies certain of those duties. The relevant statutory duties under the CA 2006 are:

- To act within powers.
- To promote the success of the company.
- To exercise independent judgment.
- To avoid conflicts of interest.
- Not to accept benefits from third parties.
- To declare an interest in a proposed transaction or arrangement.

The statutory duty replaced the corresponding fiduciary duty when the relevant provision came into force. While the new statutory duties must be interpreted and applied in the same way as the equitable principles, and regard must be had to those principles in applying them (*section 170(4), CA 2006*), including, according to the Explanatory Notes, any future developments, the equitable principles described below will only apply to directors to the extent permitted by the CA 2006.

The four key fiduciary duties

A fiduciary has an obligation to act in the interests and for the benefit of his beneficiaries.

There are four key fiduciary duties (where A is the adviser acting on B's behalf and B is his client):

No conflict

A must not place himself in a position where his own interests conflict with those of B or where there is a real possibility that this will happen. This is also known as conflict of duty or conflict of interest.

No-profit

A must not profit from his position at the expense of B. This is also known as misuse of property held in a fiduciary capacity.

This duty has been interpreted strictly. For example, where a former director of a company was held liable to account to the company for the profit he made on a contract which he had the opportunity to enter by virtue of his position as director of the company (*IDC v Cooley ((1972) 1 WLR 443).* This was so, despite the fact that he resigned his directorship to take up the contract and the company had been rejected when it offered to take up the contract itself. The director in this case was liable to account as he had allowed his interest and duty to conflict and had failed to disclose to the company the information which he had obtained before he resigned.

A less restrictive view was subsequently taken of this duty and the no-conflict rule where it was held that a director, who had been effectively excluded from all decision making and participation in his company's affairs, was not in breach of his fiduciary duty as a director when he set up another company in competition and approached former clients for work (*(1) In Plus Group Ltd (2) Interior Plus Ltd (3) Joinery Plus Ltd (4) Joinery Plus Products Ltd v John Albert Pyke [2002] EWCA Civ 370; LTL 21/3/2002))*.

Undivided loyalty

A fiduciary owes undivided loyalty to his beneficiary. Rather confusingly, this is sometimes called conflict of duty. A must not place himself in a position where his duty to another customer conflicts with his duty to B.

A consequence of the duty of undivided loyalty is that a fiduciary must make available to a customer all the information that is relevant to the customer's affairs.

Confidentiality
A must use or disclose information obtained in confidence from B for the benefit only of B.

Note that a fiduciary relationship subsists between a professional adviser and client, but it comes to an end with termination of the retainer. Thereafter, the adviser has no obligation to defend and advance the interests of the former client. The only duty to the former client which survives termination of the client relationship is a continuing duty to preserve the confidentiality of information imparted during its subsistence.
In professional relationships such as accountants, solicitors and bankers, it is implied that the client's affairs will be kept secret and not disclosed to anyone without just cause (*Parry-Jones v Law Society (1969) 1 Ch*). The limits on the duty of secrecy will depend on the circumstances peculiar to each occupation.

The continuing nature of the duty of confidentiality means that, if a professional wishes to act against a former client or for an opponent of a former client, he should only do so if he can avoid disclosing confidential information given to him by the former client. The former client can relieve the fiduciary from his duty of confidence by giving his real consent (see *Disclosure and consent*).

The above four principal duties are imposed strictly. The fiduciary duties of advisers are developed from these four basic rules.

Fiduciaries' discretion

Fiduciaries act on behalf of their beneficiaries in circumstances where the beneficiaries do not have direct control over the fiduciary's actions. Fiduciaries therefore have wide discretion in carrying out their duties. This discretion is subject to certain principles. For example, a fiduciary:

• **May not delegate without express authority.** As a general rule:

- a power involving the exercise of a personal discretion by a fiduciary cannot be delegated;
- a fiduciary has no authority to appoint a subagent except with the express or implied authority of the beneficiary; and
- where the fiduciary is selected for some employment, to which peculiar personal skill is essential or where the beneficiary reposes personal confidence in the fiduciary, that matter cannot be sub–delegated.

There are, however, exceptions to these rules, for example where the fiduciary's task is one which any reasonably competent person can do equally well or where no personal confidence is reposed in the agent. The introduction of the Trustee Act 2000 also changed the rules on delegation for trustees. Before that statute came into force, generally, a trustee was not permitted to delegate its powers unless authorised by the trust instrument or a specific statutory provision. Now under the Trustee Act 2000, trustees have powers to appoint agents, nominees and custodians; to insure trust property; and to pay professional trustees. The Trustee Act 2000 also creates a defined statutory duty of care applicable to trustees when carrying out their functions under the Trustee Act 2000 or equivalent functions under the trust instrument.

• **May not act under dictation.** A fiduciary cannot act like a puppet in accordance with the instructions of another. Dialogue between fiduciary and beneficiary is encouraged but this dialogue must not stray into dictation - the fiduciary must be free to exercise his own judgement.

• **May not bind himself as to how he will exercise his discretion in future.** Fiduciaries are unable to fetter their future discretion without the consent of the beneficiary. For example, as a general principle, a director could not validly contract (either with another director or with third parties) as to how he would vote at future board meetings. This was so even though there had been no improper purpose or motive. An exception to this rule was where directors decided that it was in the best interests of the company to enter into a contract and to carry it into effect. In such circumstances they could themselves enter into an undertaking to exercise their powers in a particular way if it was necessary for them to do so to effectuate the contract. The duty not to fetter discretion did not mean that the directors could not bind themselves to the future exercise of their powers in a particular manner - such a rule would prevent companies from entering into contracts which were commercially beneficial to them (*Fulham Football Club Ltd v Cabra Estates plc [1994] 1 BCLC 363*).

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• **Must consider whether to exercise his discretion.** The duty to consider means that the fiduciary must be prepared to act when his action would be advantageous to his beneficiaries.

• **May not exercise his powers in his own or third parties' interests.** If a fiduciary exercise his power for the sole purpose of benefiting a third party, this will be improper unless the fiduciary reasonably believed that he was furthering the beneficiary's interest by doing so. The issue of powers being exercised in the interests of third parties may arise in relation to groups of companies. If, for example, a subsidiary company is asked to provide a guarantee for a loan made to its parent company, the granting of the guarantee by the directors of the subsidiary may have meant that the directors were exercising their powers for the benefit of a third person (the parent company) and not for the benefit of their own company; there may have been no corporate benefit in the giving of the guarantee. Note that in the case of company directors, if permitted by the company's articles, they may still exercise their powers where they have a personal interest (having made the necessary declaration under section 182, CA 2006). The courts will not interfere with the director's exercise of his power unless it could be shown that he has acted in his own interests without consideration of the interests of the company.

• **Must treat beneficiaries of the same class equally.** Unless he is given power to discriminate between them, a fiduciary must treat all beneficiaries equally.

• **Must treat beneficiaries of different classes fairly.**

• **Must not act totally unreasonably**. The court retains the ability to intervene if it could be said that a fiduciary has not exercised his powers to benefit his beneficiaries but has rather acted in an overwhelmingly unreasonable and unjustifiable manner.

Remedies

The remedies for breach of fiduciary duty vary in accordance with the severity of the breach. Possible remedies include:

• **Injunction.** This is a discretionary remedy. It may be granted for breach of confidence, no conflicts or undivided loyalty. If the fiduciary misuses information by taking notes or drawings, then the courts may make an order for delivery up.

• **Setting aside of the transaction, restitution and account of profits.**

  • **Voidable transactions.** A voidable transaction may be set aside by the beneficiary, for example if the fiduciary buys or sells the beneficiary’s property on his own account *(Re Thompson’s Settlement (1986) Ch 99)*; or if the fiduciary breaches the duty of no conflicts or undivided loyalty and the beneficiary is unaware of the conflict or is misleadingly informed of it. Where the transaction is set aside, the fiduciary may still be able to claim reasonable remuneration for work he has completed *(O'Sullivan v Management Agency and Music Ltd (1985) QB 428).* Equitable compensation may be awarded in lieu of specific restitution.

• **Account of profits.** This is relevant when the fiduciary has been unjustly enriched at the expense of the claimant, for example, where he has received money belonging to the claimant. The fiduciary may have to account for profits he has made by virtue of his position or use of the beneficiary's property.

• **Damages.** Where a fiduciary fails to discharge fully his duties, he will be liable to his beneficiaries if they suffer loss as a result. If there is a contractual link between the fiduciary and the beneficiary, then damages may be available for breach of fiduciary duties. (However, the courts have allowed damages to be awarded in cases where there is no contractual link, such as damages in the tort of deceit or damages for breach of an equitable duty (*Seager v Copydex [1967] 1 WLR 929)*.

• **Disciplinary proceedings.** The fiduciary could be liable to disciplinary proceedings from an appropriate regulator or in some cases, criminal proceedings.

Modifying and controlling fiduciary duties

The methods most commonly used in the management of fiduciary duties can be divided into:

• **Contractual techniques.** Such techniques modify fiduciary duties by agreement, for example, through trade custom, the use of exclusion clauses or duty defining provisions, and by disclosure and consent.

• **Structural techniques.** These techniques are used to organise a firm in such a way as to prevent breaches arising, for example, by separation of functions, independence policies, stop and watch lists and Chinese walls. None of these methods can completely avoid the potential conflicts that arise. This does not mean, however, that fiduciaries should not go as far as they can to manage conflict by using these methods.

Trade custom

Courses of conduct which amount to a trade custom (by satisfying the requirements of notoriety, certainty, uniformity, reasonableness and an intention to affect legal rights and duties) can be incorporated into a contract. A court may hold that a trade custom which permits a fiduciary to act in a position of conflict is reasonable if the custom also provides adequate protection for the customer's interests.