➢ Questions

1. In the course of his judgment, Buxton LJ made the following point:

> as Sedley LJ emphasised in his judgment in *In Plus Group Ltd v Pyke* **[7.33]**, … the mere fact that a fiduciary has not sought to place himself in a position where his interest conflicts with his duty does not exonerate him from the obligation to perform that duty. Accordingly, it cannot be in any way conclusive that it was Mrs Watts who offered Mr Bryant the opportunity, indeed pressed it on him, rather than that he resigned in order to be free for that purpose, or asked for the opportunity once he had resigned.

Nevertheless, Buxton LJ held that, in the circumstances, it was not a breach for Bryant to accept the offer. Where is the line drawn?

2. In the course of his judgment, Rix LJ noted the trial judge's conclusions on Bryant's potential liability if he *had* been found in breach of his duties (see Rix LJ at para [46]). The trial judge noted that if Bryant had ruled himself out of working for Alliance, the work he might have done would *not* then have gone to his old company, as it had in the past—recall Alliance wanted the personal services of Bryant and Foster—it would have gone elsewhere. The significance of this, so the trial judge thought, was that in*Warman International Ltd v Dwyer* (1995) 182 CLR 544, the High Court of Australia emphasised that the rule requiring a fiduciary to account for profits should not be applied in a manner which makes it a vehicle for unjust enrichment of the claimant. It followed, according to the trial judge, that even if Bryant *had* breached his duty, there were no profits for which he was liable to account. This, however, seems to confuse claims for profits disgorgement from Bryant with claims to recover the company's loss. In assessing profits, it is irrelevant that the company could not itself have generated those profits (*Regal (Hastings)*; *Boardman v Phipps*). *Warman*, by contrast, was concerned to ensure that the *net* profits (emphasising net profits, not gross profits) of the offending venture were assessed fairly, and linked causally to the breach that generated them.

3. Would the outcome have been the same under CA 2006, given ss 170(2) and 175?

Resigning and pursuing competing opportunities in a way that breaches the conflicts rule.

[7.30] Shepherds Investments Ltd v Walters [2006] EWHC 836 (Chancery Division)

This was a claim against former directors (and employees) of Shepherds for various breaches of duty, including setting up a competing business, diversion of a business opportunity and misuse of confidential information. Walters and Hindle were directors and employees of Shepherds (Financial) Ltd ('Financial'). Simmons was a former employee and *de facto* **(p. 395)** director of Shepherds Investments Ltd ('Investments'). 'Assured' and 'PSL' were the companies through which the individuals carried on their competing business. The individuals were held to have breached their duties, and were therefore liable to account for the profits generated for the period of 'advance start' that their breach had given them, but not liable for damages because no loss was proved to have been caused by the breach.

> ETHERTON J:
>
> 82 At the heart of these proceedings is the question whether, in taking the steps which they did to establish Assured and PSL prior to their retirement from Financial and Investments, the Individual Defendants acted in breach of their duties to the companies which employed them and of which they were directors. The parties are not agreed on the legal principles and test applicable to determine that central issue.

83 It is convenient to start with what is common ground …

85 A director is under a fundamental duty to act in what he in good faith considers to be the best interests of the company. The duty was described [in] the judgment of Arden LJ in *Item Software (UK) Ltd v Fassihi* **[7.16]** [Then followed part of the extract found in that case at **[7.16]** …

87 Investments claims that … the central issue in these proceedings [ie] whether the Individual Defendants were acting lawfully in taking the steps they did for the establishment of Assured and PSL while owing fiduciary duties … is to be found in a straightforward application of the fundamental duty of a director to act in good faith in the best interests of his company. Mr Nicholls [counsel] submitted that the Individual Defendants could not have been in any doubt that it would have been in the best interests of those companies to be aware of the plans they were implementing to establish Assured and PSL.

88 Mr Nicholls placed particular weight on the reasoning and decision of Hart J in *British Midland Tool Ltd v Midland International Tooling Ltd* [2003] EWHC 466, [2003] 2 BCLC 523. In that case the claimant ('BMT') was a specialised engineering company which carried on the business of manufacturing and supplying cutting tools to the motor industry. Four of the defendants, who were directors of BMT, conceived and developed a plan, which they kept secret, to leave their jobs at BMT and set up a rival company. Following the retirement of one of those defendants as managing director of BMT, an advertisement appeared in the local paper inviting applications from fully skilled personnel for jobs with a 'specialist cutting tool manufacturer'. It gave no name and address for the prospective employer but invited applications to be sent to a box number. Shortly afterwards, the other three directors gave notice to BMT of their resignation as directors and of termination of their employment with BMT. A few days later twelve of BMT's skilled workers tendered their resignations to the company through one of those directors. The new business was set up next door to BMT's own premises. Subsequently more of BMT's employees left to join the new enterprise. A core component of BMT's business was the supply of cutting tools to Ford Motor Co. In the event BMT was unable to retain that business, and eventually it closed down. BMT brought the proceedings against the defendants alleging conspiracy to damage BMT. Hart J found in favour of BMT and held the defendants liable in damages.

89 Against that factual background, Hart J described as follows, in paragraph [81] of his judgment, the fundamental duty of a director of a company to act in good faith towards it:

> '[81] It is a fundamental duty of the director of a limited company to "do his best to promote its business and to act with complete good faith towards it": see*Scottish Co-operative Wholesale Ltd v Meyer* [1958] 3 All ER 66 at 88, [1959] AC 324 at 366 per Lord Denning. It is also his duty not to embark on a course of conduct in which his own interests will conflict with those of the company: see *Parker v McKenna* (1874) LR 10 Ch App 96 at 118 per Lord Cairns LC. He is also, like an employee, under a duty of fidelity to his company: see *Hivac Ltd v Park Royal Scientific Instruments Ltd* [1946] 1 All ER 350 at 353, [1946] Ch 169 at 174 per Lord Greene MR. On the face of it, therefore, one might think it a simple proposition that a director would be under a duty to alert his fellow board members to a nascent commercial threat to the **(p. 396)** future prospects of the company, and that the duty would be all the greater (and certainly no less) when he himself was planning to be part of that threat.'

90 Having referred to, and considered, the decision of Falconer J in *Balston Ltd v Headline Filters Ltd* [1990] FSR 385 and other cases, Hart J said as follows at paragraph [89]:

> '89 … A director's duty to act so as to promote the best interests of his company prima facie includes a duty to inform the company of any activity, actual or threatened, which damages those interests. The fact that the activity is contemplated by himself is, on the authority of *Balston's* case, a circumstance which may excuse him from the latter aspect of the duty. But where the activity involves both himself and others, there is nothing in the authorities which excuses him from it. This

applies, in my judgment, whether or not the activity itself would constitute a breach by anyone of any relevant duty owed to the company … A director who wishes to engage in a competing business and not disclose his intentions to the company ought, in my judgement, to resign his office as soon as his intention has been irrevocably formed and he has launched himself in the actual taking of preparatory steps …' …

92 Mr Quirk and Mr Kempster [counsel for the Individuals], for their part, placed particular weight on the *Balston* case. The facts of that case, so far as relevant, were that Balston manufactured and sold glass microfibre filter tubes. On 17 March 1986 the second defendant, an employee and director of Balston, gave notice of termination of his employment which expired on 11 July 1986. Prior to that date, on 14 March 1986 he had agreed to take a lease of certain business premises. His evidence was that at that time he had not decided whether to set up a business as a dealer in filtration products or as a manufacturer of filter tubes. He formally resigned his directorship on 18 April 1986. On 25 April 1986 he bought the first defendant company 'off the shelf'. On 2 May 1986 he had a telephone conversation with one of Balston's customers, in which he said that he was leaving Balston's employ and that after 12 July 1986 he would be in a position to supply filter tubes to the first defendant. On 8 May 1986 the second defendant visited the customer, and it was agreed that the customer would place an order with the first defendant for delivery from 14 July 1986 to December 1987. That order was confirmed in writing on 26 July 1986. Following the 2 May 1986 telephone call, the second defendant made active preparations for the first defendant to commence manufacture of filter tubes on or as soon as possible after 14 July 1986, including the purchase of equipment and the engaging of persons as employees of the first defendant, including certain employees and ex employees of Balston. The second defendant commenced manufacture of sample tubes for the first defendant on 13 July 1986 and showed them to the customer on 14 July 1986.

93 Falconer J held, among other things, that the second defendant was not in b[r]each of fiduciary duty as a director in not disclosing to Balston the intention to set up a business in competition or in taking such steps as he had to forward that intention prior to 18 April 1986. Nor was he in breach of his duty of fidelity as an employee, as at 18 April 1986, in forming the intention to set up a business in competition with Balston and in carrying out preparatory acts for that purpose. From 8 May 1986, however, the second defendant was in breach of his duty of good faith in being engaged in active competition with Balston for the custom of the customer, and also in approaching one of Balston's employees and offering her employment with the first defendant. The critical passage in the judgment of Falconer J, relied upon by the Defendants before me, is at p.412 as follows:

'In the statement of the overriding principle by Roskill J in the [*Industrial Development Consultants v Cooley* ("*IDC*")] case, namely "that a man must not be allowed to put himself in a position in which his fiduciary duty and his interests conflict," the conflict contemplated must be one with a specific interest of the company (or other body or person) to whom the fiduciary duty is owed, as, for example, a maturing business opportunity, as in *Canaero*, or the plaintiff's interest in the contract secured by the defendant in the *IDC* case, or a contract falling within the first class of contracts in Lord Blanesburgh's dichotomy in*Bell v Lever Bros* (page 194), or the use of some property or confidential information of the company which has come to a director as such … In my judgment an intention by a director of a company to set up business **(p. 397)** in competition with the company after his directorship has ceased is not to be regarded as a conflicting interest within the context of the principle, having regard to the rules of public policy as to restraint of trade, nor is the taking of any preliminary steps to investigate or forward that intention so long as there is no actual competitive activity, such as, for instance, competitive tendering or actual trading, while he remains a director.' …

95 The Defendants rely upon the *Balston* case as authority that the taking of preparatory steps by a director, short of actual competitive activity, is not in itself in conflict with a specific interest of the company and is not therefore in breach of fiduciary duty …

105 As the most recent in the line of relevant authority, *British Midland Tool* is binding upon me, unless I am satisfied that it is plainly wrong. Far from considering that the decision is wrong, I respectfully consider that both the decision and reasoning of Hart J in that case were correct and, in so far as there is any conflict between them and the decision and reasoning of Falconer J in *Balston*, the approach of Hart J is to be preferred.

106 In my judgment it is plain that the necessary starting point of the analysis is that it is the fiduciary duty of a director to act in good faith in the best interests of the company (*Item Software* at para [41]), that is to say 'to do his best to promote its interests and to act with complete good faith towards it', and not to place himself in a position in which his own interests conflict with those of the company (*British Midland Tool* at paragraph [81] and *CMS Dolphin Ltd v Simonet* [2001] 2 BCLC 704 at paragraph [84]).

107 It is difficult to see any legitimate basis for the 'trumping' of those duties by 'rules of public policy as to restraint of trade' as suggested by Falconer J in *Balston*at p.412. There is no reference to any such principle in any of the relevant cases prior to *Balston* … Hart J in *British Midland Tool* rejected any such principle. He said, at paragraph [89] of his judgment:

> 'It does not, furthermore, seem to me that the public policy of favouring competitive business activity should lead to a different conclusion. A director is free to resign his directorship at any time notwithstanding the damage that the resignation may itself cause the company: see *CMS Dolphin Ltd v Simonet* [2001] 2 BCLC 704 at [95] per Lawrence Collins J. By resigning his directorship he will put an end to his fiduciary obligations to the company so far as concerns any future activity by himself (provided that it does not involve the exploitation of confidential information or business opportunities available to him by virtue of his directorship).'

108 What the cases show, and the parties before me agree, is that the precise point at which preparations for the establishment of a competing business by a director become unlawful will turn on the actual facts of any particular case. In each case, the touchstone for what, on the one hand, is permissible, and what, on the other hand, is impermissible unless consent is obtained from the company or employer after full disclosure, is what, in the case of a director, will be in breach of the fiduciary duties to which I have referred or, in the case of an employee, will be in breach of the obligation of fidelity. It is obvious, for example, that merely making a decision to set up a competing business at some point in the future and discussing such an idea with friends and family would not of themselves be in conflict with the best interests of the company and the employer. The consulting of lawyers and other professionals may, depending on all the circumstances, equally be consistent with a director's fiduciary duties and the employee's obligation of loyalty. At the other end of the spectrum, it is plain that soliciting customers of the company and the employer or the actual carrying on of trade by a competing business would be in breach of the duties of the director and the obligations of the employee. It is the wide range of activity and decision making between the two ends of the spectrum which will be fact sensitive in every case. In that context, Hart J may have been too prescriptive in saying, at paragraph [89] of his judgment, that the director must resign once he has irrevocably formed the intention to engage in the future in a competing business and, without disclosing his intentions to the company, takes any preparatory steps. On the facts of *British Midland Tool*, Hart J was plainly justified in concluding, in paragraph [90] of his judgment, **(p. 398)** that the preparatory steps had gone beyond what was consistent with the directors' fiduciary duty in circumstances where the directors were aware that a determined attempt was being made by a potential competitor to poach the company's workforce and they did nothing to discourage, and at worst actively promoted, the success of that process, whereas their duty to the company required them to take active steps to thwart the process …

127 In the light of all those matters, I am quite clear that from 12 August 2003 not only had the Individual Defendants formed the irrevocable intention to establish a business which they knew would fairly be regarded by Financial and Investments as a competitor to the business carried on by SSF, but they continued to take steps to bring into existence that rival business, contrary to what they knew were the best interests of Financial and Investments, and without the consent of those companies to do so after full

disclosure of all material facts, and so in breach of their respective fiduciary duties and their obligation of fidelity. That conflict between the duties owed by the Individual Defendants to Financial (in the case of Mr Walters and Mr Hindle) and Investments (in the case of Mr Simmons), on the one hand, and the personal and private interests of the Individual Defendants, on the other hand, in the promotion of the new and rival business is exemplified by Mr Simmons' acknowledgement, in cross examination, that he found it difficult to promote 'the Shepherds product' when developing the 'new product'.

128 Further, irrespective of whether, by virtue of *Balston* and contrary to my view, there was no obligation to disclose their own individual 'preparatory' activity, I am bound by *British Midland Tool* to hold that each of the Individual Defendants was obliged, by 12 August 2003 at the latest, to disclose to Financial or Investments, as the case may be, the actual and threatened activity of the others to set up the competing business. If and so far as is necessary, like Hart J in *British Midland Tool*, I would distinguish *Balston* on the facts on the ground that the intention to compete in *Balston* does not appear to have been formed in that case prior to the resignation of the second defendant as a director. The principle that it is the duty of a director to inform the company of any actual or threatened activity of another, whether or not he himself is involved, which damages the interests of the company, and whether that activity would in itself constitute a breach by anyone of any relevant duty owed to the company, is part of the core reasoning and decision in *British Midland Tool*, which I must follow.

129 Finally, on this aspect of the case, I should record for completeness that, even if, contrary to my view, Mr Simmons was a mere employee owing no fiduciary duties to Investments, I nevertheless conclude that his conduct between 12 August 2003 and his resignation on 21 September 2003 was such as to breach his employee's duty of good faith and fidelity …

132 … As Arden LJ so clearly stated in *Item Software*, in relation to a fiduciary's duty to disclose his own misconduct to his principal, or, more generally, information of relevance and concern to his principal, the single and overriding touchstone is the fundamental duty of a director to act in what he considers in good faith to be in the best interests of the company. There is no separate and independent duty of disclosure. In the context of the director's own acts to promote a competing business, the breach of fiduciary duty is to carry out the impermissible acts of promotion without first disclosing the intention to do them and obtaining permission to do so. There is a breach because the director's conflict between his personal interest and his duty to the company has not been authorised after full disclosure to, and informed consent by, the company. In the case of the acts of his fellow directors in promoting a rival business, the breach of fiduciary duty of the director is failing to disclose matters which are of relevance and concern to the company and which, if acting in good faith in the best interests of the company, the director would disclose. Those are straightforward applications of ordinary principles of equity concerning fiduciary duties …

133 … Investments claims that the Individual Defendants have exploited for their own benefit a business opportunity, namely investment in whole life policies, of which they became aware through their employment by Financial and Investments, as the case may be, and that they are liable to account for the profit made from the exploitation of that business opportunity … [A] director who exploits after his resignation a maturing business opportunity of the company is to be treated as **(p. 399)** appropriating for himself property of the company in relation to which he had fiduciary duties. He is, accordingly, just as accountable as a trustee who retires without properly accounting for the trust property. In the case of the director, he becomes a constructive trustee[] of the fruits of his abuse of the company's property, which he has acquired in circumstances where he knowingly had a conflict of interest and exploited it by resigning from the company: *CMS Dolphin* esp. at paragraphs [84] and [96] …

146 Investments having established breach of fiduciary duty and breach of the obligation of fidelity by each of the Individual Defendants … is, on the face of it, entitled to an inquiry as to damages …

150 It is critical that, in order to establish a claim for damages, the loss allegedly suffered by Financial and Investments is linked to the Individual Defendants' unlawful acts rather than the mere fact of loss of senior management personnel and sales people. The Individual Defendants were entitled to resign. In general, there is no legal impediment to a number of employees deciding in concert to leave their employer and set themselves up in competition …

➢ Note

These ‘competition’ cases clearly depend on the fact that the competing opportunity is classed as a ‘corporate opportunity’, so these cases provide insights into the law on ‘maturing business opportunities’ and other tests. In this case, Etherton J devoted a good part of his judgment (not extracted here) to the factual assessment of this issue.

➢ Questions

1. Of the four ‘key factors’ identified in *Canaero* (earlier), which were missing in *Island Exports Finance Ltd v Umunna* and in *Balston Ltd v Headline Filters Ltd* (earlier)? Do the more modern cases such as *Foster Bryant Surveying Ltd v Bryant, Savernake Property Consultants Ltd* **[7.29]**, *Shepherds Investments Ltd v Walters* **[7.30]** and *In Plus Group Ltd v Pyke* **[7.33]** adopt the same set of ‘key factors’?

2. Jane is a director of three unrelated investment companies. She is approached in confidence by two young scientists whose company needs a major injection of finance to develop a newly discovered drug. After investigating the project, she forms the view that it is likely to be a highly profitable venture for any one of the three companies. What advice should Jane be given?

3. Do these cases represent the current state of the law, applying CA 2006 ss 170(2), 175 and 239?

4. Now that we have a statutory formulation of the duties, should these cases be brought under CA 2006 s 175 (conflicts of interest) or CA 2006 s 172 (good faith for the success of the company)? Does it matter? Are the remedies different?

Remedial options when defaulting directors pursue corporate opportunities—remedies against the director and against any corporate vehicle used to pursue the opportunity.

[7.31] CMS Dolphin Ltd v Simonet [2001] 2 BCLC 704, [2002] BCC 600 (Chancery Division)

Ball and Simonet formed an advertising agency, CMS Dolphin Ltd (CMSD), financed by Ball and run by Simonet. It was permanently underfunded, and tensions grew between Ball and Simonet. On 16 April 1999, Simonet resigned as managing director and set up in business, first under the trade name Millennium, and later as Blue (GB) Ltd (Blue), with Patterson who had previously been chief executive of a company in the WPP group, the well-known **(p. 400)** international advertising agency. Following Simonet’s resignation, all the staff of CMSD left to join Simonet and Patterson, and the principal clients whom Simonet had introduced to CMSD switched their business to Millennium/Blue.

LAWRENCE COLLINS J:

2. The case raises (among other questions) the existence and applicability of the principle … that a director is disqualified from usurping for himself or diverting to a company with which he is associated a maturing business opportunity of his company not only while he is still a director, but also even after his resignation, when the resignation may fairly be said to have been prompted or influenced by a wish to acquire for himself the opportunity sought by the company …

96. In my judgment the underlying basis of the liability of a director who exploits after his resignation a maturing business opportunity of the company is that the opportunity is to be treated as if it were property of the company in relation to which the director had fiduciary duties. By seeking to exploit the opportunity

after resignation he is appropriating for himself that property. He is just as accountable as a trustee who retires without properly accounting for trust property. In the case of the director he becomes a constructive trustee of the fruits of his abuse of the company's property, which he has acquired in circumstances where he knowingly had a conflict of interest, and exploited it by resigning from the company.

Duty to account

97. In many cases, an account of profits will be a more advantageous remedy than equitable compensation, since the actual profits obtained by the director may be higher than the damages for the loss of opportunity suffered by the company, particularly where (as in *Industrial Development Consultants Ltd v. Cooley* and*Canadian Aero Service Ltd. v. O'Malley*) the company had little or no prospect of obtaining the benefit of the opportunity. The fiduciary is liable for the whole of the profit. There are no firm rules for determining which is the relevant profit: see *Hospital Products Ltd. v. United States Surgical Corp*. (1984) 156 C.L.R. 41, at 110, *per*Mason J. Where, as here, the business (to use a neutral term, not distinguishing between Simonet and Blue) is not restricted exclusively to the performance of contracts which were obtained from CMSD, the fiduciary should be accountable for the profits properly attributable to the breach of fiduciary duty, taking into account the expenses connected with those profits and a reasonable allowance for overheads (but not necessarily salary for the wrongdoer), together with a sum to take account of other benefits derived from those contracts. For example, other contracts might not have been won, or profits made on them, without (e.g.) the opportunity or cash flow benefit which flowed from contracts unlawfully obtained. There must, however, be some reasonable connection between the breach of duty and the profits for which the fiduciary is accountable.

Effect of use of corporate vehicle

98. In this case … Blue is hopelessly insolvent … although it is said to have made profits from the contracts in question. Mr Simonet has personally made no profits, and claims that there is therefore nothing for which he should account. According to CMSD, he remains accountable for the profits. Does it make a difference to the remedy for an account of profits whether the director exploits the opportunity personally, or through a partnership, or through a company controlled by him? In particular, is there a remedy against the director where the profits are made by a company against which there is no effective remedy, because for reasons unconnected with the relevant contracts it is hopelessly insolvent? The question is one of practical importance because the case of an individual trading as such (as distinct from through a corporate vehicle) is rare in purely commercial transactions. In this case the trading was done through the Millennium partnership for about two weeks, and then through Blue …

100. Where the business is put into a company which is established by the directors who have wrongfully taken advantage of the corporate opportunity, it was held in*Cook v. Deeks* **[7.22]** that both the directors and the company are liable to account for profits …

(p. 401) 101. In *Canadian Aero Service Ltd. v. O'Malley* it was clearly no impediment to the liability of the directors to account for profits that the contract was obtained by a company which they had formed to exploit the opportunity …

102. Neither *Cook v. Deeks* nor *Canadian Aero Service Ltd. v. O'Malley* was treated a case of piercing or lifting the corporate veil. The directors and their company were each liable to account. Some cases have held the director liable to account on the basis that he was to be identified with the company on a piercing or lifting the corporate veil rationale. In *Gencor ACP Ltd. v. Dalby* [2000] 2 B.C.L.C. 734, Rimer J. held a director liable for the dishonest diversion of business opportunities which had been channelled into an offshore company which was wholly owned and controlled by him, and which was no more than a shell. It was simply a creature company and was to be identified in equity with the director. So also an Australian court treated a company into which contracts had been channelled as the alter ego of the director: *Green v. Bestobell Industries Pty* [1984] W.A.R. 32, 40.

103. Is the position different where (as here) the corporate vehicle genuinely carries on business, and has real premises and a staff? Even in such a case it is possible that the piercing the corporate veil approach

may be justified if the company was incorporated to perpetrate what must be regarded as wrongdoing close to fraud: *cf*. *Re H* [1996] 2 B.C.L.C. 500. But I do not think that it is necessary to resort to piercing or lifting the corporate veil, since *Cook v. Deeks* shows clearly (as does *Canadian Aero Service Ltd. v. O'Malley*) that the directors are equally liable with the corporate vehicle formed by them to take unlawful advantage of the business opportunities. The reason is that they have jointly participated in the breach of trust.

104. Nor in my judgment does it make a difference whether the business is taken up by the corporate vehicle directly, or is first taken up by the directors and then transferred to a company …

Remedies

140. As regards the allegation of unlawful diversion of the business opportunities of CMSD, CMSD is entitled (at its option) to equitable compensation or an account of profits … from Simonet, not only in respect of profits made by him in the short period in which he and Patterson traded as Millennium, but also for the period they traded as Blue. What Mr Simonet diverted was not simply such business as gave rise to profits in the period that Millennium traded. He diverted the benefit of the existing Argos and DFB contracts and the opportunities that were associated with them and with the Reebok connection. CMSD does not seek an account for any period beyond 1999, and there are therefore no difficult issues of connection and causation … It is implicit in this exercise that Mr Simonet is entitled to credit for the expenses incurred by Millennium/Blue in earning the profits including a reasonable proportion of overhead, and I will hear argument as to whether that should include salary paid to Mr Simonet and Mr Patterson, and as to whether any other points of principle will arise on the taking of an account …

142. … If there had been no effective remedy in relation to the allegations of breach of fiduciary duty, I would have held that the breach of the duty of fidelity (which would have involved the acquisition of the Argos, Reebok and DFB accounts) would have justified the remedy of an account of profits and not simply damages. In *Att. Gen. v. Blake* [2000] 3 W.L.R. 625, 639 (H.L.) Lord Nicholls said that one of the exceptional circumstances which would justify a restitutionary remedy for breach of contract was the characterisation of a contractual obligation as fiduciary and a finding that the claimant has a legitimate interest in preventing the profit-making activity of the defendant. This is such a case …

➢ Note

Lawrence Collins J suggests that the corporate opportunity (here, the 'maturing business opportunity') is treated as the company's property, and trustee-type remedies follow if the directors misuse that property. Note that not every opportunity is a 'corporate opportunity'; it is still necessary to decide first whether pursuit of *this* venture by the directors is in breach of their duty of loyalty. Remember, too, that in making this assessment it is irrelevant that pursuit of the opportunity by the company itself might have been legally or practically impossible.

(p. 402) ➢ Questions

1. The defaulting director has to account for the profits made in breach of his or her duty to avoid conflicts. A constructive trust over the whole business venture, forever, is rarely warranted—this is not the proper measure of the 'profit' that the director has made *from the breach* (but see *Cook v Deeks* **[7.22]**, *Regal (Hastings)* **[7.23]**). If the director accounts in money, the net profits generated by the opportunity are usually demanded for a period of time. Which of the cases extracted earlier take this approach? How is the time period assessed? How are the 'net profits' assessed—in particular, why do some cases allow the directors to claim a salary, and others do not?

2. The orthodox equitable remedy awarded against directors (or other fiduciaries) who engage in conflicts of

interest is to strip profits from them, not to award compensation to the company for breach of a 'duty' (now see CA 2006 ss 175 and 178). Breach of the obligation to act bona fide and in the interests of the company, by contrast, attracts the remedy of equitable compensation (now see CA 2006 ss 171, 172 and 178). Does this mean, in practice, that there is always a choice of profits disgorgement or compensation in any case of corporate opportunities? Can the injured company have *both* ?

3. When the defaulting director uses a new company to pursue the opportunity, Lawrence Collins J suggested both the director and the company would be liable, either because the corporate veil might be lifted (presumably only in appropriate circumstances) or because the company had knowingly participated in a breach of duty. Does the choice of legal analysis affect the *quantum* of liability of either the director or the new company? Are the director and the new company each liable for the *same amount* (whether profits disgorgement or compensation)? Is this appropriate? What is the outcome if the new company is a 'real' company with innocent shareholders?

Statutory exception under s 175(4)(a)

Situations that 'cannot reasonably be regarded as likely to give rise to a conflict'.

Board authorisation can be given where there *is* a conflict of interest (s 175(4)–(6)). But, in addition, s 175(4)(a) provides that the duty is not infringed if the situation cannot reasonably be regarded as likely to give rise to a conflict of interest. Some situations will fall very clearly into this category. But the next case is controversial: it deals with the difficult question of whether an opportunity, once declined by the company, may then be taken up by one of the directors on his own account, without any notification to or approval by the other directors or the shareholders. There are no UK cases adopting this approach.

[7.32] Peso Silver Mines Ltd v Cropper (1966) 58 DLR (2d) 1 (Supreme Court of Canada)

The board of directors of the appellant company Peso was approached by an outsider named Dickson, who wished to sell to it 126 prospecting claims near to the company's own mining territories. The proposal was rejected by the company after bona fide consideration by the board. Later, a syndicate was formed by Dr Aho, the company's geologist, to purchase Dickson's claims. The syndicate included Cropper, a director of Peso. A company called Cross Bow Mines Ltd was incorporated by the syndicate for the purpose. Cropper had taken part in the earlier decision of Peso's board to reject Dickson's proposal. Control of Peso later passed to a company referred to as 'Charter', which caused this action to be brought, claiming that Cropper was accountable to the company for the Cross Bow shares which he had thus **(p. 403)** obtained. The Supreme Court of Canada decided that he held them on his own behalf and was not bound to account.[60]

> The judgment of the court (CARTWRIGHT, MARTLAND, JUDSON, RITCHIE and HALL JJ) was delivered by CARTWRIGHT J: On the facts of the case at bar I find it impossible to say that the respondent obtained the interests he holds in Cross Bow and Mayo by reason of the fact that he was a director of the appellant and in the course of the execution of that office.
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> When Dickson, at Dr Aho's suggestion, offered his claims to the appellant it was the duty of the respondent as director to take part in the decision of the board as to whether that offer should be accepted or rejected. At that point he stood in a fiduciary relationship to the appellant. There are affirmative findings of fact that he and his co-directors acted in good faith, solely in the interests of the appellant and with sound business reasons in rejecting the offer. There is no suggestion in the evidence that the offer to the appellant was accompanied by any confidential information unavailable to any prospective purchaser or that the respondent as director had access to any such information by reason of his office. When, later, Dr Aho approached the appellant it was not in his capacity as a director of the appellant, but as an individual member of the public whom Dr Aho was seeking to interest as a co-adventurer.
>
> The judgments in the *Regal* case **[7.23]** in the Court of Appeal are not reported but counsel were good enough to furnish us with copies. In the course of his reasons Lord Greene MR said: 'To say that the

company was entitled to claim the benefit of those shares would involve this proposition: Where a board of directors considers an investment which is offered to the company and bona fide comes to the conclusion that it is not an investment which their company ought to make, any director, after that resolution is come to and bona fide come to, who chooses to put up the money for that investment himself must be treated as having done it on behalf of the company, so that the company can claim any profit that results to him from it. That is a proposition for which no particle of authority was cited; and goes, as it seems to me, far beyond anything that has ever been suggested as to the duty of directors, agents, or persons in a position of that kind.'

In the House of Lords, Lord Russell of Killowen concluded his reasons with the following paragraph: 'One final observation I desire to make. In his judgment Lord Greene MR stated that a decision adverse to the directors in the present case involved the proposition that, if directors bona fide decide not to invest their company's funds in some proposed investment, a director who thereafter embarks his own money therein is accountable for any profits which he may derive therefrom. As to this, I can only say that to my mind the facts of this hypothetical case bear but little resemblance to the story with which we have had to deal.'

I agree with Bull JA[61] when after quoting the two above passages he says: 'As Greene MR was found to be in error in his decision, I would think that the above comment by Lord Russell on the hypothetical case would be superfluous unless it was intended to be a reservation that he had no quarrel with the proposition enunciated by the Master of the Rolls, but only that the facts of the case before him did not fall within it.'

As Bull JA goes on to point out, the same view appears to have been entertained by Lord Denning MR in *Phipps v Boardman*.[62]

If the members of the House of Lords in *Regal* had been of the view that in the hypothetical case stated by Lord Greene the director would have been liable to account to the company, the elaborate examination of the facts contained in the speech of Lord Russell of Killowen would have been unnecessary.

(p. 404) The facts of the case at bar appear to me in all material respects identical with those in the hypothetical case stated by Lord Greene and I share the view which he expressed that in such circumstances the director is under no liability. I agree with the conclusion of the learned trial judge and of the majority in the Court of Appeal that the action fails …

➢ Notes

1. *Boardman v Phipps* [1967] 2 AC 46, HL, referred to in the extract, was not a company law case, but is of interest as an application of the principle of *Regal (Hastings) Ltd v Gulliver* **[7.23]**. B, a solicitor, and P, acting together as agents for the trustees of an estate, attended the annual general meeting of a company in which the estate had a minority holding of shares. Later, they obtained information about share prices from that company. They formed the opinion that the company could be made more profitable and, acting honestly and without concealment (but not having first obtained the 'informed consent' of all the trustees), used their own money to bid for and eventually to acquire a controlling interest in it. The estate itself could not have made the bid without the trustees committing a breach of trust, and in any case it had no funds available for the purpose. Ultimately, they succeeded in making considerable profits for both themselves and the estate from capital distributions on their respective holdings of shares. By a 3:2 majority, the House of Lords held that they must account to the trust for the profit which they had made from their own investment: the profit had been made by reason of their fiduciary position as agents and by reason of the opportunity and the knowledge which had come to them while acting in that capacity. The remedy was proprietary (the order granted by Wilberforce J was reinstated). However, the House of Lords did think it proper to decree that the defendants should be paid 'on a liberal scale' for their work and skill.

2. In *Thermascan Ltd v Norman* [2011] BCC 535 (Ch), David Donaldson QC held that, once the contractual basis for a restraint not to compete with the company has lapsed, the restraint does not persist under CA

2006 s 175. In this case, the company provided services to customers using infrared technology, in particular for surveying commercial buildings to reveal hotspots caused by electrical faults. A former director launched his own business to offer thermal imaging surveys and was successful in canvassing orders from the claimant company's former clients. It was held that these possible new surveys more than eight months later cannot 'properly be described as a business opportunity in the course of maturing' [19] as at the director's resignation. Although it is not necessary to demonstrate that formal negotiations were underway; the learned judge found it hard to see how a claim can succeed without it being demonstrated that there had been at least some form of significant discussion of the potential business at the time of resignation.

➢ Questions

1. Can the decision in the *Peso Silver Mines* case be reconciled with *Boardman v Phipps* (earlier), *Aberdeen Rly Co v Blaikie Bros* **[7.34]** and the passage from *Keech v Sandford* quoted in *Regal (Hastings) Ltd v Gulliver* **[7.23]** ?

2. Is *Peso Silver Mines* likely to be embraced in the UK, even with the introduction of s 175(4)(a)?

Conflicts of duty and duty: competing directorships

Section 175(7) makes it clear that conflicts of duty and duty (ie conflicting duties of loyalty owed to two different principals) are within the remit of s 175.

The controversial House of Lords authority in this area is *Bell v Lever Bros Ltd* [1932] AC 161. It treats directors more leniently than employees are treated by employment law; it holds **(p. 405)** that directors are not under an obligation to refrain from competing with their companies or from becoming directors of rival companies, although this conclusion assumes that the first company has no concern in the contracts of the second, and that in earning the profit on those contracts the director has not made use of either the property or the confidential information belonging to the first company (see the opinion of Lord Blanesburgh).

The next case is unusual, but airs some of the concerns in this area. The extract is long, but this is a rare Court of Appeal authority on a difficult issue.

[7.33] In Plus Group Ltd v Pyke [2002] EWCA Civ 370, [2003] BCC 332 (Court of Appeal)

The company, In Plus Group Ltd, was controlled by two men, Pyke and Plank, its only directors and members. When the business relationship between Pyke and Plank deteriorated, Pyke was entirely excluded from the management of the company. He was refused access to financial records, no longer received his monthly payments from the company and his office was relocated without consultation or notice. With neither job nor income, Pyke established a new company and started doing business with Constructive, one of the company's major clients. The claimants argued that this competition with the company amounted to a breach of Pyke's fiduciary duties to it, and they sought an account of Pyke's profits.

> BROOKE LJ: … There is no completely rigid rule that a director may not be involved in the business of a company which is in competition with another company of which he was a director. A rather startling illustration of this proposition can be seen in the case of *London and Mashonaland Exploration Co Ltd v New Mashonaland Exploration Co Ltd* [1891] WN 165. Lord Mayo was a director and chairman of the board of directors of the first company which was incorporated for the purpose which its name suggests. He never in fact acted as a director, or attended a board meeting, or agreed, either expressly or in the articles of association, not to become a director of any similar company. Four months later the second company was formed for the same purpose. The first company had had some success with a share prospectus advertising Lord Mayo's name as director and chairman, and it took umbrage when it saw its rival's