EXAMINING THE INCIDENCE OF FIDUCIARY DUTIES IN EMPLOYMENT

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I. Introduction

The dictionary defines loyal as "faithful or steadfast in allegiance".[1] The majority of cases that reach the courts where it is claimed that employees have acted disloyally involve employees competing with their employer or former employer.[2] Examples include employees: approaching an employer's clients or customers with a view to doing business with them;[3] diverting business opportunities to competitors rather than securing the opportunities for their employer;[4] soliciting suppliers of their employer in preparation for commencing a competing business;[5] and compiling valuable information acquired during employment for use in competition with their employer.[6]

Under the common law, an employee's faithfulness and allegiance to an employer is compelled by a contractual duty of loyalty implied into the employment contract. The duty is generally referred to as a duty of good faith and fidelity.[7] Competitive activity by an employee during his or her employment will amount to a breach of the duty. Breach of the duty of good faith and fidelity may give an employer a right to dismiss the employee and/or damages for loss suffered.

Fiduciary law potentially provides employers with an additional mechanism to hold errant employees to account for disloyal behaviour. Framing a claim in fiduciary law may offer an employer a number of advantages. In particular, breach of a fiduciary duty of loyalty opens the door to a broader range of remedies than breach of contract, including an account of profits and proprietary remedies.[8]

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1 *Shorter Oxford English Dictionary* (6th ed, Oxford University Press, Oxford, 2007) at 1650.

2 A.J. Geare "An Employee's Duty of Loyalty: New Zealand Law and Practice" (1999) 20 Comparative Labor Law and Policy Journal 283 at 287.

3 *Walden v Barrance* [1996] 2 ERNZ 598 (EMC).

4 *Bradford Trust Ltd v Paul Edward Roebeck Ltd* (2006) NZELR 635 (HC). *Bradford Trust Limited v Roebuck* ERA Auckland AA60/08, 26 February 2008.

5 *Big Save Furniture Ltd v Bridge* [1994] 2 ERNZ 507 (CA).

6 *Ongley Wilson Real Estate Ltd t/a Manawatu First National v Burrows* [1999] 1 ERNZ 231 (EMC).

7 See *Robb v Green* [1895] 2 QB 315 at 320 per A.L. Smith LJ.

8 See generally Andrew Butler "Fiduciary Law" in Andrew Butler (ed) *Equity and Trusts in New Zealand* (2nd ed, Thomson Reuters, Wellington, 2009) 471 at 569-574.

New Zealand courts have been reticent to view the employment relationship as giving rise to fiduciary duties, unless such duties arise in the employee's capacity as an office holder in an organisation, such as when the employee is a director.[9] Case law suggests that fiduciary duties will not arise for "ordinary", non-office holding employees who only owe a contractual duty of good faith and fidelity.

This article argues that New Zealand courts have been too quick in rejecting the idea that the employment relationship, in itself, may give rise to fiduciary duties. Too much attention seems to have been placed on the position of an employee within a company hierarchy. It is argued that New Zealand courts should be more ready to recognise that an employment relationship, in itself, may result in the incidence of fiduciary duties by applying a fact-based approach that examines the duties that an employee has undertaken.

Part one of this article lays the framework for the argument. It commences by explicating the general approach to fiduciary liability and defines the nature of fiduciary duties. An employee's common law duty of good faith and fidelity is also described and contrasted. Part two outlines and critiques the predominant approach of New Zealand courts to the incidence of fiduciary duties in employment. Part three, drawing on more recent New Zealand Supreme Court decisions exploring the incidence of fiduciary duties in commercial arrangements, argues for a more fact-based analysis of an employee's duties. Part three also examines some persuasive English decisions that may additionally support a fact-based approach to the incidence of fiduciary duties in employment. Part four explores the significance of making a fiduciary law claim against a disloyal employee. Part five concludes.

II. Two Concepts of Loyalty

A. Fiduciary Obligations

Under conventional doctrine, fiduciary duties are owed when there is a fiduciary relationship in existence. Consequently, courts generally approach a claim for fiduciary liability by first examining whether the relationship between the parties is fiduciary in nature. If a fiduciary relationship is found, a court will examine whether the fiduciary has breached a fiduciary duty.[10]

Historically, courts have adopted a "status" approach to determine whether a particular relationship is fiduciary in nature.[11] Under this approach the type of legal actor involved determines whether the relationship will be considered

9 The Companies Act 1993, s 126 contains a wide and comprehensive definition of the term "director". See the commentary by Susan Watson "The Board of Directors" in John Farrar (ed) *Companies and Securities Law in New Zealand* (Brookers, Wellington, 2008) at 299-322. This article does not directly consider the duties of de jure or de facto directors.

10 See Paul B Miller "A Theory of Fiduciary Liability" (2011) 56 McGill Law Journal 235 at 239-240

11 James Edelman "When Do Fiduciary Duties Arise?" (2010) 126 LQR 302 at 305.

fiduciary. Extending by analogy from the paradigm fiduciary relationship of trustee and beneficiary, courts have presumed other relationships fiduciary because of the inherent nature of the duties owed by particular types of legal actors.[12]

Courts have also classified relationships as fiduciary using a "fact-based" approach. Under this approach courts have determined that the factual characteristics of a relationship justify it being classified as fiduciary. It has also been recognised that relationships that typically do not give rise to fiduciary duties "may nevertheless have a fiduciary dimension".[13] Fiduciary duties may arise in respect of a part of a relationship, and not in respect of other parts.[14]

No test or formula has received universal acceptance in defining what makes a relationship, or part of a relationship, fiduciary in nature.[15] The lack of a universally accepted test or formula betrays deeper schisms as to the purpose of fiduciary law. A number of theories have been put forward to explain whether or not a relationship is fiduciary in nature.[16] A variety of hallmarks have been suggested, including power and discretion,[17] vulnerability,[18] control of property,[19] and voluntary undertakings to another.[20] Conceptual uncertainty, though, remains.[21]

Therefore, before considering when an employment relationship may be considered to give rise to fiduciary duties, it may be useful to first articulate the nature of the fiduciary duties imposed on those in a fiduciary relationship. As Birks has suggested: [22]

> Among the many questions that can be asked of any legal obligation, or its correlative right, two are especially important. The first goes to content. What does the obligation require? The second seeks the causative event. From what facts does it arise? It is often difficult to formulate a crisp answer to the second question unless one has a firm grip on the answer to the first.

12 These include the relationships of director and company, *Regal (Hastings) Ltd v Gulliver* [1967] 2 AC 134 (HL) at 147-149; solicitor and client, *Sims v Craig Bell & Bond* [1991] 3 NZLR 535 (CA) at 543; partner and partner, *Helmore v Smith (No 1)* (1887) 35 Ch D 436 at 444.

13 *Chirnside v Fay* [2006] NZSC 68, [2007] 1 NZLR 433 at [72].

14 *New Zealand Netherlands Society "Oranje" Inc v Kuys* [1973] 2 NZLR 163 (PC) at 166.

15 *Chirnside v Fay* [2006] NZSC 68, [2007] 1 NZLR 433 at [75].

16 See JC Shepherd "Towards a Unified Concept of Fiduciary Relationships" (1981) 97 LQR 51 for a summary of different theories and Butler, above n 8, at 560-561. See also L.S. Sealy "Fiduciary Relationships" (1962) Cambridge Law Journal 69 at 74-79 for an attempt at categorising fiduciary relationships.

17 Shepherd, above n 16, at 53-56.

18 *Watson v Dolmark Industries Ltd* [1992] 3 NZLR 311 (CA) at 315 per Cooke P describing vulnerability as a "cardinal feature" of a fiduciary relationship.

19 *Reading v Attorney-General* [1949] 2 KB 232 (CA) at 236. See also Robert Flannigan's "limited access" thesis in Robert Flannigan "The Boundaries of Fiduciary Accountability" (2004) 84 Canadian Bar Review 35.

20 See Edelman, above n 11, at 302.

21 See Sir Anthony Mason "Themes and Prospects" in Paul D Finn (ed) *Essays in Equity* (Law Book Company, North Ryde (NSW), 1985) 242 at 246.

22 PBH Birks "The Content of Fiduciary Obligation" (2000) 34 Israel Law Review 3 at 4.

Loyalty has been identified as the "distinguishing obligation" of a fiduciary.[23] A fiduciary obligation of loyalty is generally considered to comprise two elements.[24] First, a fiduciary must not place himself or herself in a position where the principal's interests and his or her own personal interests conflict. Secondly, a fiduciary must not make an unauthorised profit by reason of his or her position as a fiduciary. These "no conflict" and "no profit" fiduciary principles are negative in nature in that they prohibit a fiduciary from contravening them. Drawing on the proscriptive nature of these fiduciary principles,[25] commentators have emphasized that a fiduciary obligation of loyalty insists on selflessness. For example, Finn suggests the aim of fiduciary law is to secure the paramountcy of one party's interests in a relationship.[26] Worthington describes fiduciary loyalty as an obligation of self-denial.[27] Such a characterization of fiduciary loyalty highlights a requirement of undivided or "single-minded loyalty"[28] on the part of the fiduciary. In *Breen v Williams* Gaudron and McHugh JJ explained:[29]

> Duty and self-interest, like God and Mammon, make inconsistent calls on the faithful. Equity solves the problem in a practical way by insisting that fiduciaries give undivided loyalty to the persons whom they serve.

"Unselfish and undivided"[30] fiduciary loyalty is exacted in a prophylactic manner. Thus, being in a position of conflict is enough. A fiduciary's honesty, or the fact that the principal has not been harmed, does not excuse liability. A fiduciary wishing to avoid liability for acting in a situation of conflict must make "full and frank disclosure of all material facts",[31] and obtain the informed consent of his or her principal. This strict prophylactic approach aims to prevent a fiduciary from being "swayed by interest rather than by duty, and thus prejudicing those whom he is bound to protect".[32]

23 *Bristol and West Building Society v Mothew* [1998] Ch 1 at 18 per Millet LJ.

24 *Bray v Ford* [1896] AC 44 at 51. *Chan v Zacharia* (1984) 154 CLR 178 at 198-199. See generally Matthew Conaglen *Fiduciary Loyalty: Protecting the Due Performance of Non-Fiduciary Duties* (Hart Publishing, Oxford and Portland, Oregon, 2010) at 39-40.

25 In *Chirnside v Fay* [2006] NZSC 68, [2007] 1 NZLR 433 at [80] Tipping J expressed a fiduciary obligation of loyalty in proscriptive terms. However, Jessica Palmer "Fiduciaries and Remedies" [2007] NZLJ 36 at 38 has suggested that the fiduciary obligation of loyalty can still be understood as being able to apply prescriptively consistent with *Bank of New Zealand v New Zealand Guardian Trust Co Ltd* [1999] 1 NZLR 664 (CA) i.e., that the fiduciary must act in the interests of another and that the duty of loyalty entails more than the prophylactic duties not to profit nor enter into conflicts of interest.

26 Paul D Finn "Contract and the Fiduciary Principle" (1989) 12 University of New South Wales Law Journal 76 at 83.

27 Sarah Worthington "Fiduciaries: When is Self-Denial Obligatory" [1999] Cambridge Law Journal 500 at 502.

28 *Bristol & West Building Society v Mothew* [1998] Ch 1 at 18.

29 *Breen v Williams* (1996) 186 CLR 71 at 108 (Gaudron and McHugh JJ).

30 Finn, "Contract and the Fiduciary Principle", above n 26, at 83.

31 *New Zealand Netherlands Society "Oranje" Inc v Kuys* [1973] 2 NZLR 163 (PC) at 168.

32 *Bray v Ford* [1896] AC 44 at 51.

B. Employment Obligations

Under the common law employees also owe a duty of loyalty to their employer. The most important aspect of an employee's loyalty is the duty of good faith and fidelity.[33] This duty is generally understood to be the product of implied contractual terms, although its origin may well be equitable.[34] The duty of fidelity is considered so integral to the employment relationship that it is implied as a matter of judicial policy into all employment contracts.[35] Goddard CJ has remarked that the central prohibition under the duty of fidelity is "misuse of the employer's property for the employee's benefit".[36] This prohibition reflects a policy of protecting the economic interests of the employer that can be traced to the earliest cases concerning the implied duty of fidelity.

Robb v Green[37] remains a useful starting point in understanding the duty.[38] An employee, while employed by the plaintiff, secretly copied a list of the names and addresses of the plaintiff's customers with the intention of using the information in competition once he left the employment of the plaintiff. The employee was found to be in breach of an implied term of his contract. The trial judge, Hawkins J, had a "very decided opinion" that in every contract of service there was an implied obligation on an employee that he or she:[39]

> …shall honestly and faithfully serve his master; that he shall not abuse his confidence in matters appertaining to his service, and that he shall, by all reasonable means in his power, protect his master's interests in respect to matters confided to him in the course of his service.

Hawkins J was quick to clarify that he did not intend to convey that while employed a person may not undertake preparatory activities for his or her own business. Hawkins J stated that such activities are permissible provided the employee does not fraudulently undermine his or her employer by breaking the confidence reposed in him or her.[40]

33 See *Mazengarb's Employment Law* (LexisNexis) at [1028].

34 See Paul D Finn, *Fiduciary Obligations* (Law Book Company, Sydney, 1977) at 237 who suggests that while the duty of fidelity is both a common law and equitable duty, courts have preferred to use the language of implied terms: "an equitable term being found vaguely subversive in the contract lawyer's stronghold of employment law". See also *Concut v Worrell* (2000) 176 ALR 693, 700-701 [26] (Gleeson CJ, Gaudron and Gummow JJ).

35 B Hepple "Employee Loyalty in English Law" (1998) 20 Comparative Labor Law and Policy Journal 205 at 206.

36 *Walden v Barrance* [1996] 2 ERNZ 598 (EMC) at 616.

37 *Robb v Green* [1895] 2 QB 1.

38 As noted in *SGS New Zealand Limited v Nortel (1998) Ltd* HC Whangarei CIV 2006-448-384, 20 December 2007 at [27].

39 *Robb v Green* [1895] 2 QB 1 at 10-11.

40 Ibid, at 15.

Hawkins J's judgment was upheld on appeal,[41] where A.L. Smith LJ observed "I think that it is a necessary implication which must be engrafted on such a contract that the servant undertakes to serve his master with good faith and fidelity".[42] Lord Esher MR said the duty would be breached by conduct which any person of ordinary honesty would look upon as dishonest and a dereliction of an employee's duty to act towards the employer in good faith.[43]

The duty of fidelity overlaps with a second implied term: a mutual duty of trust and confidence. In *Woods v WM Car Services (Peterborough) Ltd* Browne-Wilkinson J described this duty as requiring parties to an employment relationship to refrain from conducting themselves "in a manner calculated or likely to destroy or seriously damage the relationship of confidence and trust between the employer and employee".[44]

From an employee's perspective, a duty of trust and confidence would appear to add little to an employee's obligation of loyalty required by the duty of fidelity.[45] However, as Anderson notes, there is some evidence of the duty of trust and confidence being used by New Zealand courts to reinforce and extend the duty of fidelity.[46] Moreover, despite Lord Esher MR's comments in *Robb v Green,* the New Zealand Court of Appeal has signalled that it is not necessary to prove dishonesty on the part of the employee to find a breach of the duty of fidelity.[47] Rather than dishonesty, the undermining of trust and confidence in the employment relationship has become a touchstone. Thus, in *Tisco Ltd v Communication and Energy Workers Union*, the Court of Appeal characterized a breach of the duty of fidelity as:[48]

> Any conduct by an employee which is likely to damage the employer's business, for instance by impairing its goodwill, or to undermine significantly the trust which the employer is entitled to place in the employee, could constitute a breach of duty. The duty of fidelity and good faith carries with it a duty not to undermine the relationship of trust and confidence.

The Court of Appeal's dicta linking trust and confidence to fidelity suggest that an employee's common law duty of fidelity might go beyond a negative prohibition against conduct that harms the employer's business enterprise.[49] Indeed, some New Zealand case law has suggested that the duty of fidelity requires an employee to proactively report actions or events that may cause harm to the business interests of the employer. For example, in

41 *Robb v Green* [1895] 2 QB 315.
42 Ibid, at 320.
43 Ibid, at 316.
44 *Woods v WM Car Services (Peterborough) Ltd* [1981] ICR 666 at 670.
45 *Malik v Bank of Credit and Commerce International SA (in liquidation)* [1998] AC 20 (HL) at 46 per Lord Steyn.
46 Gordon Anderson "Good Faith in the Individual Employment Relationship in New Zealand" (2011) 32 Comparative Labor Law and Policy Journal 685 at 696.
47 *Big Save Furniture Ltd v Bridge* [1994] 2 ERNZ 507 (CA) at 517.
48 *Tisco Ltd v Communication and Energy Workers Union* [1993] 2 ERNZ 779 (CA) at 782.
49 See Anderson, above n 46, at 697.

Interchem Agencies v Morris it was alleged that an employee had improperly taken his employer's agency contract while employed as a sales manager and had failed to pass on concerns and material information about the agency to his employer.[50] On appeal, the Court of Appeal rejected a submission that the employee did not breach his duty of fidelity because he was approached by the customer, and not vice versa. The Court found that an employee's duty of fidelity required him to report the likelihood of a customer moving away.[51]

A proactive element to an employee's duty of fidelity aligns with the statutory expression of the duty of good faith imposed into all employment relationships by the Employment Relations Act 2000 (Act).[52] Section 4(1)(b) of the Act states that the obligation of good faith requires parties in an employment relationship not to do anything, whether directly or indirectly, to mislead each other, or that is likely to mislead or deceive each other. Section 4(1)(A)(b) of the Act states the duty of good faith requires parties in an employment relationship to be active and constructive in maintaining an employment relationship in which the parties are responsive and communicative.

Yet, given the existence and pervasiveness of the implied duty of fidelity, the influence of the statutory duty of good faith on employee loyalty would appear to be relatively minor.[53] As Anderson argues, in practical terms the main impact of the statutory duty is on the exercise of an employer's discretions and powers.[54] In a case where an employee's actions were claimed to amount to a breach a contractual duty of fidelity and the statutory duty of good faith, the High Court has observed that:[55]

> … it is unlikely that the statutory duty of good faith would impose any duty greater than the contractual duty of fidelity and can properly be seen as subsumed within the duty of fidelity.

50 *Interchem Agencies v Morris* [2002] 2 ERNZ 256 (EMC).

51 *Morris v Interchem Agencies Ltd* [2003] 1 ERNZ 93 (CA) at [38]. See also *Waikanae Holdings (Gisborne) Limited v Smith* [2005] ERNZ 267 (EMC) at [47].

52 Employment Relations Act 2000.

53 Anderson, above n 46, at 721.

54 Ibid, at 714-717 and 721.

55 *SGS New Zealand Limited v Nortel (1998) Ltd* HC Whangarei CIV 2006-448-384, 20 December 2007 at [30]. This comment was in response to the defendant's submission that breach of the statutory duty of good faith would not amount to breach of contract for purposes of the tort of inducement to breach contract.

C. Fiduciary Loyalty and Fidelity Loyalty

It appears that a fiduciary obligation of loyalty and an employee's contractual duty of fidelity involve "much the same idea".[56] However, despite their conceptual similarity, it is contended that there is an important point of distinction between the duty of fidelity and a fiduciary duty of loyalty. While the precise content of the duty of fidelity is decided on the facts of each case,[57] it is contended that, as a general rule, the duty of fidelity does not require an employee to pursue the best interests of his or her employer at the expense of his or her own self-interest.[58] Generally speaking, an employee's duty of fidelity may enable an employee to act in his or her self-interest, provided that in his or her action or decision he or she has positive regard to the legitimate interests of the employer.[59] In some circumstances an employee may be required to withhold the pursuit of his or her individual interests. However, this is not the same as requiring an employee to completely subordinate his or her interests to the selfless pursuit of his or her employer's best interests - as a fiduciary is required to do.

Thus, absent a restraint of trade, an employee is free to take steps in his or her own time to prepare for a new business that will compete with the employer, provided such preparatory activities do not harm the employer or involve use of the employer's property, resources or confidential information.[60] In a similar vein, although dependent on the facts and nature of employment, the duty of fidelity may not prohibit an employee taking on a spare time job for another employer, unless such spare time activities inflict harm on the employer or destroy the relationship of trust and confidence.[61]

As a result of these general principles it is contended that a distinction arises between fidelity and fiduciary loyalty on the basis that the duty of fidelity does not typically prohibit an employee from being in a position where self-interest and duty conflict.[62] In contrast, and as advocated above, the characteristic obligation of a person owing a fiduciary obligation of loyalty

56 *Schilling v Kidd Garrett* [1977] 1 NZLR 243 (CA) at 270 per Cooke J. Compare Robert Flannigan "The [Fiduciary] Duty of Fidelity" (2008) 124 LQR 274 who argues that the duty of fidelity is a "conceptual malformation". By looking at the jurisprudential roots of the duty of fidelity, Flannigan argues that the orthodoxy that the duty of fidelity is distinct from a fiduciary duty of loyalty has only come about as a result of "truncated citation of authority".

57 *Hivac Ltd v Park Royal Scientific Instruments Ltd* [1946] 1 Ch 169 at 174.

58 Compare the more strict view of Chilwell J in *PCA of New Zealand v Evans* (1987) 1 NZELC 95,412 (HC) at 95,426.

59 See Paul D Finn "The Fiduciary Principle" in TG Youdan (ed) *Equity, Fiduciaries and Trusts* (Carswell, Toronto, 1989) 1 at 4 contrasting what he describes as the "good faith standard" with the "fiduciary standard".

60 See *Balston Ltd v Headline Filters* [1990] FSR 385 and *Marsden Providors (1988) Ltd v Cotterill* (1989) 2 NZELC 97,094 (HC).

61 Such as where the employee moonlights for a competitor, see *Hivac Limited v Park Royal Scientific Instruments Ltd* [1946] Ch 169 at 178. See also *Nova Plastics Ltd v Froggatt* [1982] IRLR 146.

62 *British Midland Tool Ltd v Midland International* [2003] EWHC 466 (Ch) at [94].

is to pursue the interests of another and to eschew the pursuit of his or her own self-interest. A fiduciary is plainly prohibited from putting himself or herself in a position where self-interest and duty conflict.[63]

It will be demonstrated that the nature of this unselfish and undivided fiduciary loyalty has important consequences in ascertaining when such an obligation should be owed by an employee in addition to his or her contractual duty of fidelity. However, the next section first considers the approach of New Zealand courts to the incidence of fiduciary duties in employment.

III. Do Employees Owe Fiduciary Duties in New Zealand?

A. The Predominant Employment Court View

A line of Employment Court cases suggest that an employee, other than an officer of a company, will not owe fiduciary duties to his or her employer.[64] A clear example of the Employment Court's stance on employee's owing fiduciary duties is *Franklin Veterinary Service (1977) Ltd v Jerram*.[65] Mr Jerram was a team leader of the employer's specialist referral veterinarian practice (FVSL). FVSL asserted that by reason of his position, Mr Jerram owed FVSL the duties of a fiduciary, including what it described as "perfect fairness", "full candour and disclosure", "not to act against FVSL's best interests", and "not to allow his personal interests to come into conflict with his obligations to FVSL".[66] It was alleged that Mr Jerram, whilst employed, breached such fiduciary duties by making deliberate preparations to compete with the employer.

When the matter was heard in the Employment Court, Colgan J observed that as Mr Jerram was not a shareholder, director or officer of the company it was wrong for the Employment Relations Authority below to elevate his employment obligations to the duties of a fiduciary.[67] Colgan J stated:[68]

> A third example is the apparent assumption by the Authority that Mr Jerram owed the obligations of a fiduciary to his employer. On the facts of the case and the law, this is a very dubious proposition. Although I accept that the parties owed each other reciprocal duties of trust, confidence and good faith commensurate

63 *Bray v Ford* [1896] AC 44 at 51.

64 *Korbond Industries Ltd v Jenkins* [1992] 1 ERNZ 1141 (EMC) at 1150. *BFS Marketing Ltd v Field* [1992] 2 ERNZ 1105 (EMC) at 1120. *Predict (NZ) Ltd v Morgan (No. 1)* [1993] 2 ERNZ 867 (EMC) at 875. *Nedax Systems NZ Ltd v Waterford Security Ltd* [1994] 1 ERNZ 491 (EMC) at 500. *Birthcare Auckland Ltd v McFarland* [2000] 1 ERNZ 674 (EMC) at [24]-[28].

65 *Franklin Veterinary Service (1977) Ltd v Jerram* ERA Auckland AA40/01; AEA222/01, 4 May 2001. Challenge of the Employment Relations Authority decision to the Employment Court reported at [2001] ERNZ 157.

66 *Jerram v Franklin Veterinary Service (1977) Ltd* [2001] ERNZ 157 (EMC) at [42].

67 Ibid, at [52].

68 Ibid, at [52].

> with the particular position held by the employee and the nature of the business enterprise, it is something else altogether to elevate these obligations to the significantly more onerous duties of a fiduciary.

Colgan J observed that a long line of New Zealand cases supported the view that Mr Jerram, in his position, was not subject to the duties of a fiduciary.[69]

Another example is provided by *Nedax Systems NZ Ltd v Waterford Security Ltd*.[70] Two senior employees, one of whom was also a director, left to work for a competitor that soon thereafter acquired the work of the employer's major client. In considering the employer's claims for breach of fiduciary duty against both defendants, Goddard CJ observed:[71]

> I find it possible, also, to discard at the outset the causes of action, even if directed solely at the second and third defendants, that are based on alleged breaches of a supposed fiduciary duty. An employee is not a trustee. If the second and third defendants solicited the business of Telecom whilst still employed by the plaintiff, that activity, as is common ground, will be caught by ordinary principles of employment law…
>
> …The second defendant was plainly a fiduciary while he held the office of director. It would be most unfair, however, to saddle the third defendant with any fiduciary obligations. He was not an officer of the company. He may have been a relatively senior employee in the plaintiff's small organisation but the level of his salary package does not indicate that he was a highly paid and highly trusted employee.

The clear thrust of Employment Court authority suggests that if fiduciary duties are to arise in an employment context, an employee must have some other status, such as being a director of the company.[72]

69 The cases referred to were *Cable Price Corp Ltd v McFadyen* HC Christchurch CP 37-91, 8 March 1991; *Korbond Industries Ltd v Jenkins* [1992] 1 ERNZ 1141 (EMC); *Gibson v Allegra Corp Ltd* HC Auckland CP1546/91, 5 February 1992; *Nedax Systems NZ Ltd v Waterford Security Ltd* [1994] 1 ERNZ 491 (EMC); *Sun Products NZ Ltd v Hunter* EC Auckland AC109/99, 22 December 1999.

70 *Nedax Systems NZ Ltd v Waterford Security Ltd* [1994] 1 ERNZ 491 (EMC).

71 Ibid, at 500.

72 This is a view shared by some employment law commentators, see Jo Appleyard and Peter Churchman, "Claims by Employers against Employees" in *2006 New Zealand Law Society Employment Law Conference Papers* (New Zealand Law Society, Wellington, 2006) 219 at 233; Susan Rowe "Breaches of Fiduciary Duties by Senior Employees" [2005] *Employment Law Bulletin* 156; Susan Rowe "Breaches of Fiduciary Duties by Senior Employees: Postscript" [2006] *Employment Law Bulletin* 165. But compare Stephen Langton and Philip Skelton "I say Fidelity…You Say Fiduciary… Fidelity, Fiduciary, Fiduciary, Fidelity, Let's Call the Whole Thing Off: A Practical Look at the Obligations of the Departing Employee and the Litigation Options Available to the Ex-Employer to Prevent Unfair Competition" in *2008 New Zealand Law Society Employment Law Conference Papers* (New Zealand Law Society, Wellington, 2008) 203 at 214; and Butler, above n 8, at 545.

B. Views Expressed in the High Court

The High Court has been more accepting of the incidence of fiduciary duties in employment than the Employment Court. Some cases have suggested that fiduciary duties may arise where persons occupy senior employment roles. In *C E Elley Ltd v Wairoa-Harrison,*[73] and *SSC & B Lintas NZ Ltd v Murphy*,[74] it was held there was an arguable case that senior employees owed fiduciary duties.[75] Both cases cited with approval *Canadian Aero Service Ltd v O'Malley*[76] for the proposition that "top management" may owe fiduciary duties.

In *Bradford Trust Ltd v Paul Edward Roebuck Ltd* Venning J granted an employer injunctive relief against former employees for breach of their fiduciary duties, also citing *Canadian Aero Service* with approval.[77] Venning J observed that although not directors, the employees were in senior and responsible positions.[78] In *Transnet NZ Ltd v Dulhunty Power*, Keane J, citing *Bradford Trust* with approval, held that there was an arguable case that a senior, non-office holding, employee breached a limited fiduciary duty in diverting business opportunities for the benefit of associated parties.[79]

Canadian Aero Service, and its citation by the High Court in the above cases, is significant in suggesting that seniority may be a determinant of when fiduciary duties will be owed by employees. In *Canadian Aero Service* two defendants, holding the positions of President and Vice President of the company, usurped a business opportunity the company was pursuing. In considering whether the employees owed fiduciary duties, Laskin J drew a distinction between senior "agent like" employees and mere employees.[80] In Laskin J's view "mere employees" only have a duty to respect trade secrets and the confidentiality of customer lists.[81] However, the defendants were top management, holding senior positions and charged with responsibilities that

73 *C E Elley Ltd v Wairoa-Harrison* (1987) 8 IPR 423.

74 *SSC & B Lintas NZ Ltd v Murphy* (1981) 1 NZCLC 98,384.

75 *C E Elley Ltd v Wairoa-Harrison* (1987) 8 IPR 423 at 432; *SSC & B Lintas NZ Ltd v Murphy* (1981) 1 NZCLC 98,384 at 98,390 – 98,392. Although later in *Korbond Industries Ltd v Jenkins* [1992] 1 ERNZ 1141 at 1149-1150 Colgan J limited the ratio of both cases. In the first case, Colgan J noted that the defendants to the application for an interim injunction were both directors and employees. In the second case, Colgan J noted that when the case went to full trial (*SSC & B Lintas NZ Ltd v Murphy (No. 2)* [1986] 2 NZLR 436) Pritchard J appeared to decide the case on the basis of the duty of fidelity and the word "fiduciary" did not appear in the judgment.

76 *Canadian Aero Service Ltd v O'Malley* (1973) 40 DLR (3d) 371 (SCC) [*Canadian Aero Service*].

77 *Bradford Trust Ltd v Paul Edward Roebuck Ltd* (2006) 4 NZELR 635 (HC) ["*Bradford Trust*"].

78 Ibid at [49].

79 *Transnet NZ Ltd v Dulhunty Power* [2007] ERNZ 379 (HC) at [41].

80 Canadian Aero Service, above n 76, at 381.

81 Ibid, at 381.

were far removed from "obedient servants".[82] Accordingly, the defendants were subject to fiduciary duties similar to those owed to a corporate employer by a director.[83]

C. Critique of Both Approaches

It is suggested that neither the approach of the Employment Court, nor the approach by the High Court, are sound or particularly helpful in determining when fiduciary duties are owed by employees. Turning first to the Employment Court's approach that requires an employee to be an officer of the company in order to be subject to fiduciary duties, there are two main problems.

First, it is contended that restricting the incidence of fiduciary duties solely to employees who are also directors is too limiting. The term "director" is defined widely under the Companies Act 1993, which potentially results in a wide range of persons not formally appointed as directors being found to be de facto directors.[84] Nevertheless, corporate structures vary and some large companies vest significant decision making power and responsibility with employees who may not be de jure or de facto directors. Even in smaller companies, some employees may be in positions to carry out important facets of a company's business on its behalf without being appointed a director.[85]

If a fiduciary duty of loyalty is imposed on a director to prevent the director favouring his or her own self-interest and thus prejudicing his or her duty to protect the interest of the company, there seems no reason in principle why non-director employees, who occupy positions of significant power and influence, should not be held to owe fiduciary duties. As with other principles of equity, fiduciary law is flexible and has to be applied "to a great diversity of circumstances".[86]

The difficulty with the wider notion of extending fiduciary duties to those employees who, while not directors, are officers of the company is that it is not clear where to draw the line. It may be tolerably clear that employees in the position of Chief Executive Officer or Chief Financial Officer may be considered officers of a company.[87] However, beyond employees in these positions,[88] a clear demarcation on the basis of status or title is not evident.

The difficulty is compounded because under the Companies Act 1993 the term "officer" is not defined. Under the Companies Act 1955 the term officer was defined to include a manager.[89] But even then there are various kinds of

82 Ibid, at 381.
83 Ibid, at 381-382.
84 See n 9 above.
85 Andrew Stafford QC and Stuart Ritchie *Fiduciary Duties: Directors and Employees* (Jordan Publishing, Bristol, 2008) at 84.
86 *Boardman v Phipps* [1967] 2 AC 46 (HL) at 123 per Lord Upjohn.
87 See Rowe, "Breaches of Fiduciary Duties by Senior Employees", above n 72.
88 Who may be deemed directors under s 126 of the Companies Act 1993 in any event, see n 9 above.
89 Companies Act 1955, s 2.

managers, and the label "manager" itself would not appear to be very helpful. For example, in a contractual dispute case, it was alleged that affidavits were defective because they were sworn by a person who was not an officer of the company as contemplated by the High Court Rules in force at the time.[90] Master Venning suggested that the position and responsibility of *the* manager of a private company was sufficient to constitute a person as an officer, but the definition of officer may not stretch to *a* manager of a private company.[91] A similar difficulty in determining whether a person holding a managerial position is an "officer" may occur in employment cases.

The second problem is that reference to an employee being a director or an office holder invites an "all or nothing" approach to the existence of a fiduciary relationship.[92] An all or nothing approach contradicts Lord Browne Wilkinson's warning against concluding that all fiduciaries owe the same duties in all circumstances.[93] It may also prompt courts to overlook that fiduciary duties may arise in respect of part of an employment relationship.[94] For example, some non-office holding employees may have roles that still entail significant decision-making power, authority or responsibility. Employees in such positions may have some duties that require them to act in the sole interests of their employer and eschew their own self-interest. Other employees, including those that are not in significant positions of responsibility, may also have duties that give them access to the employer's property or business opportunities,[95] and as a result require them to forego their own self-interest.

Turning to the High Court's approach that seems to place weight on the seniority of the employee, the problem with this approach is that it is not supported by principle. As Flannigan has identified, other persons in traditional fiduciary relationships, such as directors and trustees, cannot avoid the imposition of fiduciary duties by claiming humble character.[96] There is no such thing as a junior director or a junior trustee. A distinction between junior and senior employees, on that basis alone, is arbitrary and may present a misleading picture of the incidence of fiduciary duties.

Rather than using seniority, or using an office holder demarcation to decide whether it is appropriate for fiduciary law to apply, it is contended that an examination of the factual nature of the employer/employee relationship and the duties an employee has undertaken provides a more principled framework for determining the incidence of fiduciary duties. Such a fact-based

90 In *Durham Developments Ltd v Hempseed* (1997) 11 PRNZ 378 (HC); aff'd *Hempseed v Durham Developments Ltd* [1998] 3 NZLR 265 (CA).

91 *Durham Developments Ltd v Hempseed* (1997) 11 PRNZ 378 (HC) at 383.

92 Stafford & Ritchie, above n 85, at 111.

93 *Henderson v Merrett Syndicates Ltd* [1995] 2 AC 145 at 206 per Lord Brown-Wilkinson.

94 *New Zealand Netherlands Society Oranje Inc v Kuys* [1973] 2 NZLR 163 (PC) at 166.

95 Arguably as in *Transnet NZ Ltd v Dulhunty Power* [2007] ERNZ 379 (HC) and *Bradford Trust v Paul Edward Roebuck Ltd* (2006) 4 NZELR 635 (HC).

96 Robert Flannigan "The Fiduciary Accountability of Ordinary Employees" (2006) 13 Canadian Labour & Employment Law Journal 375 at 378.

approach is supported by more recent New Zealand Supreme Court decisions concerning the incidence of fiduciary duties in commercial relationships and persuasive overseas case law.

IV. Rethinking the Incidence of Fiduciary Duties in Employment

A. A Fact-Based Approach

In *Chirnside v Fay* the Supreme Court considered the incidence of fiduciary duties in a pre-contractual joint venture.[97] Tipping J, in a joint judgment with Blanchard J, postulated that all fiduciary relationships, whether status or fact-based, are characterized by an entitlement of one party to place trust and confidence in the other.[98] As a result of such trust and confidence, "that party is entitled to rely on the other party not to act in a way which is contrary to the first party's interests".[99] Tipping J's test is similar to tests of legitimate expectation,[100] or reasonable expectation,[101] of self-interest subjugation that have found favour by other New Zealand appellate courts. Arguably, Tipping J's approach in *Chirnside v Fay* cements a "legitimate entitlement" test as the prevailing one in New Zealand law.[102]

In the course of his judgment Tipping J expressly rejected the submission that it is necessary for there to be an *express* undertaking to act in the interests of another before an entitlement of fiduciary loyalty arises.[103] However, Tipping J additionally observed that where fiduciary duties arise where there is no express undertaking to act for or on behalf of another, such an undertaking is "at the very least" implicit from the circumstances.[104] And for Tipping J the "true principle…resides in the idea that the circumstances must be such that one party is entitled to repose and does repose trust and confidence in the other".[105]

Unfortunately, *Chirnside v Fay* provides no real practical guidance as to what circumstances will create such a legitimate entitlement. It is suggested that Tipping J's test does not mean the mere reposing of trust or placing of confidence is conclusive of the existence of a fiduciary relationship.[106] Rather,

97 *Chirnside v Fay* [2006] NZSC 68, [2007] 1 NZLR 433.

98 Ibid, at [80]. Gault J also concurred with Tipping J's reasons on the existence of a fiduciary relationship, at [51]–[52].

99 Ibid, at [80].

100 *Arklow Investments v Maclean* [2000] 2 NZLR 1 (PC) at 4.

101 *DHL International (NZ) v Richmond Ltd* [1993] 3 NZLR 10 (CA) at 23.

102 This test appears to accord with that suggested by Finn, see n 108 and accompanying text below.

103 *Chirnside v Fay* [2006] NZSC 68, [2007] 1 NZLR 433 at [85] and [87].

104 Ibid, at [85].

105 Ibid, at [85].

106 *Hospital Products Ltd v United States Surgical Corporation* (1984) 156 CLR 41 at 69 per Gibbs CJ.

the reposing of trust and placing of confidence by one party in another must be such to give rise to entitlement of fiduciary loyalty. And fiduciary loyalty, as explained above,[107] can be characterized as requiring a fiduciary to act in the sole interest of another party, and denying the pursuit of his or her own self-interest. Thus, as Finn puts it:[108]

> [A] person will be a fiduciary in his relationship with another when and insofar as that other is entitled to expect that he will act in that other's or in their joint interest to the exclusion of his own several interest.

Framed in this way, it is contended that the incidence of fiduciary duties based on a legitimate entitlement test is best understood as being determined by reference to all the circumstances of the case. Trust, confidence, dependence, vulnerability, discretion, influence or power may all be relevant in assessing the legitimacy of an entitlement that one person act in the other's sole interest, to the exclusion of his or her own.[109] For example, the greater the degree of trust and confidence reposed in a person the more likely that a legitimate entitlement of fiduciary loyalty will arise. Similarly, the greater the degree of power reposed in the person and/or the greater degree of vulnerability of the principal the more likely such an entitlement will arise.[110]

B. The Role of Contract in Applying a Fact-Based Approach in Employment

When parties are in a relationship governed by contract, examining the nature of parties' contractual arrangements is a crucial first step in evaluating the circumstances that may give rise to a legitimate entitlement of loyalty.[111] The importance of examining the contractual arrangements between the parties is particularly significant in employment, as without a contract there is no employment relationship.[112] The employment contract, and/or possibly the course of dealings between the parties,[113] will primarily frame the context of undertaking of the employee and provides the foundation for any legitimate entitlement to arise.

107 See n 25-30 and accompanying text above.

108 Paul D Finn "The Fiduciary Principle", above n 59, at 54.

109 Paul D Finn Ibid, at 46-48. See also *Hodgkinson v Simms* (1994) 117 DLR (4th) 161 (SCC) at 176.

110 See also Edelman, "When Do Fiduciary Duties Arise?" above n 11, at 317-318.

111 *Paper Reclaim Ltd v Aotearoa International Ltd* [2007] NZSC 26, [2007] 3 NZLR 169 at [31] per Blanchard J.

112 Although this need not be in any particular form, thus for example although the Employment Relations Act 2000, s 65(1) requires employment agreements need to be in writing, the Court of Appeal in *Warwick Henderson Gallery Ltd v Weston* [2006] 2 NZLR 145 (CA) held that an oral employment agreement may still be enforceable.

113 *Birtchnell v Equity Trustees Executors and Agency Co Ltd* (1929) 42 CLR 384 at 408 per Dixon J where it was explained the character of an undertaking may be ascertained by the express terms of the agreement of the parties and from the relevant course of dealings pursued by the parties.

While the employment contract provides the primary foundation for the incidence of fiduciary duties, the employment contract also potentially circumscribes whether they will arise. This is because, as stated in *Hospital Products v United States Surgical Corporation,* the law is reluctant to superimpose fiduciary duties on top of the contractual obligations of parties, unless such fiduciary duties conform to and are consistent with the terms of the contract.[114]

In *Hospital Products,* instead of the distributor using its best efforts to promote the sale of the overseas manufacturer's products in Australia, it surreptitiously copied the manufacturer's product and put into effect a plan to sell the copied products in competition. The overseas manufacturer bought a claim for breach of fiduciary duty seeking a variety of relief, including a declaration that the distributor held certain assets on constructive trust in its favour.

In considering the claim for breach of fiduciary duty, all members of the Australian High Court predicated their judgment by reference to the contractual arrangements between the parties. The fact that the distributor was at liberty to make business decisions and take action by reference to its own interest was inconsistent with the existence of the claimed fiduciary relationship.[115] For the majority of the Australian High Court, the arrangement between the parties did not indicate any obligation on the distributor to disregard its own interests in favour of the interests of the overseas manufacturer.[116]

It is contended that the same principles are instructive in an employment context. A close examination of an employee's undertaking, whether express or implied, will be required to ascertain whether the circumstances create a legitimate entitlement of fiduciary loyalty. While acknowledging that determining what facts give rise to a fiduciary expectation cannot be answered in the abstract, a few general observations can be ventured.

First, an employee's contractual duties, whether express or implied, must place the employee in a position where he or she must act solely in the interests of the employer, and not in his or her own self-interest. The purpose for which relevant duties are assigned to an employee is likely to be a relevant consideration in making this assessment. For example, where an employee's duties are for the purpose of securing business opportunities for a company, an employer is likely to repose a significant amount of trust and confidence

114 *Hospital Products v United States Surgical Corporation* (1984) 156 CLR 41 at 97 per Mason J.

115 Ibid, at 72-73 per Gibbs CJ, at 97-98 per Mason J, at 118-119 per Wilson J, at 122-124 per Deane J, at 137- 147 per Dawson J.

116 Mason J found that the distributor had a fiduciary relationship with the USSC limited to its product goodwill as in respect of some activities the distributor could not act solely in its interests without reference to the manufacturer, at 101. Deane J held that there was no fiduciary relationship between the parties but that USSC was entitled to an order that the distributor account as constructive trustee on the basis that such equitable relief was "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", at 124.

in the employee that the employee act in the employer's best interest, and not in his or her own.[117] Similarly, where an employee is given control of an employer's property, there may often be a legitimate entitlement for the employer to place trust and confidence in the employee not to act in a way which is contrary to the employer's interest.

However, that is not to say that an employer's labelling of an employee as a "fiduciary" in an employment contract will be sufficient to convince a court that fiduciary obligations are owed. Courts are likely to look to the substance of the arrangement rather than the form.[118] There may also be, depending on the circumstances, an argument that such a contractual term would be void having regard to the restraint of trade doctrine.[119]

Secondly, whether there is a legitimate entitlement of fiduciary loyalty will be coloured by the level of control over an employee's duties stipulated in an employment contract. As Mason J observed in *Hospital Products*, a contractual term may be so precise in its regulation of what a party can do that there is no relevant area of discretion remaining and therefore no scope for fiduciary duties to arise.[120] Where an employer has contractually reduced or eliminated an employee's discretion to carry out his or her employment duties, it may be unlikely that fiduciary duties will arise in respect of those duties.

Conversely, if the obligations of an employee are open-ended, there is a greater likelihood that fiduciary duties may arise in relation to them.[121] Open-ended duties may be carried out in different ways. Many different circumstances may arise when an employee is carrying out such duties.[122] As a result, an employer is likely to place more trust and confidence in the employee to carry out open-ended duties. An employer is also more likely to be vulnerable to an employee's exercise of discretion in carrying out such duties. In such circumstances, it may be more likely for a legitimate expectation of fiduciary loyalty to arise.

Sims points out that the issue of contractual control is not a question of whether the employer actually controlled the employee's activities but whether the employer had the ability do so under the contract.[123] She argues that an "employer who fails to utilize the means of supervision provided by the contract of employment should not be able to regain control by relying on fiduciary obligations".[124] However, the mere fact that the option of

117 See for example *Industrial Development Consultants v Cooley* [1972] 1 WLR 443.

118 Stafford & Ritchie, above 85, at 130-131.

119 Ibid, at 130-131.

120 *Hospital Products Ltd v United States Surgical Corporation* (1984) 156 CLR 41 at 98, citing *R.H. Deacon & Co Ltd v Varga* (1972) 30 DLR (3d) 653; affirmed (1973) 41 DLR (3d) 767.

121 See also *Counties Manukau Pacific Trust v Manukau City Council* [2009] 2 NZLR 260 (HC) at [91].

122 V Sims "Is Employment a Fiduciary Relationship" (2001) 30 *Industrial Law Journal* 101 at 107.

123 Richard Nolan "The Legal Control of Directors' Conflicts of Interest in the United Kingdom: Non-executive Directors Following the Higgs Report" (2005) 6 *Theoretical Inquiries in Law* 413 at 422-423.

124 Ibid, at 107.

contractual regulation was open to the parties to protect themselves,[125] may not necessarily be fatal to a fiduciary claim.[126] The better view may be that contractual regulation should be *one* of the considerations that help determine whether a fiduciary expectation is legitimate in all the circumstances.[127]

Thirdly, and aligned to the issue of discretion, the ability for an employer to supervise an employee's conduct may affect the legitimate entitlement test. Circumstances that allow an employee little scope to exercise his or her duties in an unsupervised manner will often be a relationship where insufficient trust and confidence is placed in an employee for a fiduciary duty of loyalty to arise. In contrast, it may be contended that, where there is scope for an employee to carry out his or her duties in an unsupervised manner, the employer will be particularly vulnerable and more trust and confidence is likely to be placed in an employee. Therefore, there may be a greater likelihood for there to be a legitimate entitlement of fiduciary loyalty.

Finally, even where the overall nature of the employment relationship is not fiduciary in nature, there may be aspects of an employee's role which do trigger a fiduciary duty of loyalty. In *Amaltal Corporation Ltd v Maruha Corporation* the Supreme Court held that fiduciary obligations arose in the context of tax and accounting functions carried out in a joint venture.[128] The Court considered that fiduciary duties arose as one party was entitled to rely on the other for loyal performance of tax and accounting functions, even though the whole relationship between the parties was not fiduciary in character.[129] Application of these principles in an employment context suggests that an employee, not particularly senior or trusted, may still have some duties that require that employee to act solely in the employer's best interests to the exclusion of his or her own interests. In such circumstances, there may be a legitimate entitlement of fiduciary loyalty in respect of part of an employee's role.

125 See also *Hospital Products Ltd v United States Surgical Corporation* (1984) 156 CLR 41 at 147 per Dawson J.

126 See *LAC Minerals Ltd v International Corona Resources* (1989) 61 DLR (4th) 14 (SCC) at 41 per La Forest J.

127 Conaglen, above n 24, at 266 (emphasis in original).

128 *Amaltal Corporation Ltd v Maruha Corporation* [2007] NZSC 40, [2007] 3 NZLR 192 at [24].

129 Ibid, at [24].

C. Persuasive Overseas Case Law

Buoyed by the *University of Nottingham v Fishel* case, some English judges appear to be adopting a more fact-based approach to the incidence of fiduciary duties in employment.[130] *Fishel* has been cited only once in New Zealand in an interim injunction proceeding.[131] Yet, it is contended *Fishel* is generally consistent with the fact-based approach adopted by the Supreme Court judgments highlighted above, and warrants close examination by New Zealand Employment Courts in the future.

In *Fishel* a leading embryologist, Dr Fishel, was employed by the plaintiff as a full-time scientific director of its infertility clinic. During his employment, Dr Fishel regularly undertook work at private clinics abroad for remuneration without the consent of the plaintiff, in breach of his employment contract. Dr Fishel also sent other employee embryologists under his supervision to work at the private clinics in breach of their employment contracts. Dr Fishel was paid directly by the overseas clinics and made his own arrangements as to remuneration with the employee embryologists. When Dr Fishel left to set up his own infertility clinic, the university alleged that he was in breach of his contractual duties and fiduciary duty.

In considering a claim for breach of fiduciary duty, Elias J opined that employment is not typically a fiduciary relationship as "its purpose is not to place the employee in a position where he is obliged to pursue his employer's interests at the expense of his own".[132] Elias J observed that if fiduciary obligations are to arise in employment they:[133]

> … result from the fact that within a particular contractual relationship there are specific contractual obligations which the employee has undertaken which have placed him in a situation where equity imposes these rigorous duties in addition to the contractual obligations.

Elias J explained that the employment duties of good faith, loyalty and mutual trust and confidence should not be equated with a fiduciary duty.[134] Unlike a fiduciary duty, employment duties of good faith, loyalty or trust and confidence do not require a person to subjugate his or her interests

130 *Nottingham University v Fishel* [2000] ICR 1462 [*Fishel*]. Subsequent English and Australian cases have cited *Fishel* with approval, see *Hydra Plc v Anatasi* [2005] EWHC 1559 (QB) at [61]. *Crowson Fabrics Ltd v Paul Rider* [2007] EWHC 2942 (Ch) at [81]. *Hanco ATM Systems Ltd v Cashbox ATM Systems Ltd* [2007] EWHC 1599 (Ch) at [63]. *Cobbetts LLP v Hodge* [2009] EWHC 786 (Ch) at [89]-[92]. *Lonmar Global Risks Ltd v West & Ors* [2010] EWHC 2878 (QB) at [149]-[152]. *Francis v South Sydney District Rugby League Football Club Ltd* [2002] FCA 1306 at [267].*Woolworths Ltd v Olson* [2004] NSWSC 849 (22 September 2004) at [214]; *Victoria University of Technology v Wilson* (2004) 60 IPR 392 at [145]; *Michael Wilson and Partners Limited v Robert Colin Nicholls & Ors* [2009] NSWSC 1033 (6 October 2009) at [71].

131 *A C Nielsen (New Zealand) Ltd v Pappafloratos* [2003] 1 ERNZ 363 (EMC).

132 *Nottingham University v Fishel* [2000] ICR 1462 at 1491.

133 Ibd, at 1491.

134 Ibid, at 1492-1493.

to another.[135] Accordingly, for Elias J, if fiduciary duties are to arise in an employment relationship, it is necessary to identify the duties undertaken by an employee and "to ask whether in all the circumstances he has placed himself in a position where he must act solely in the interests of his employer".[136]

On the facts of the case, Elias J found that Dr Fishel did not owe fiduciary duties in respect of his work conducted outside of the university, as Dr Fishel did not have a contractual duty to seek or obtain work overseas.[137] There was no duty of loyalty with which Dr Fishel's interests conflicted. However, it was held that Dr Fishel did owe fiduciary duties in respect of his duty to direct and control the university employee embryologists.[138] Dr Fishel placed himself in a position where there was a potential conflict between his specific duty to direct the embryologists to work in the interests of the university and his own financial interests in directing their work abroad.[139]

In *Helmet Integrated Systems v Tunnard* the English Court of Appeal approved the approach of Elias J in *Fishel.*[140] Mr Tunnard was a salesman at Helmet Integrated Systems Ltd (HISL), a company that produced and sold protective equipment. While continuing to work for HISL, Mr Tunnard conceived an idea for a modular protective helmet and took various steps to advance his idea towards a marketable product, including obtaining funding, and commissioning design drawings. Mr Tunnard subsequently resigned from HISL and incorporated his own company to sell the new helmet in competition with HISL.

HISL's claims against Mr Tunnard for infringement of intellectual property rights, breach of fidelity and breach of fiduciary duty were unsuccessful at first instance.[141] On appeal, the matter turned on whether Mr Tunnard's preparatory activities amounted to a breach of a fiduciary duty owed to HISL. HISL's counsel argued that Mr Tunnard's contractual undertaking formed the basis for the existence of a fiduciary duty. In making the assessment of whether Mr Tunnard's preparatory activities were legitimate Moses LJ stated that:[142]

> The first task…is to identify the nature of the employee's obligations. Once they have been identified, the court is then in a proper position to discern whether the activities of an employee undertaken in pursuance of a plan to be fulfilled on his departure is in breach of his duty to his employer or not.

Mr Tunnard's job specification included a duty to "advise on competitor activity and pricing structures". It was argued that this duty required Mr Tunnard to advise HISL on competitor activity, whether undertaken by a

135 Ibid, at 1493.
136 Ibid, at 1493.
137 Ibid, at 1496.
138 Ibid, at 1498.
139 Ibid, at 1498.
140 *Helmet Integrated Systems v Tunnard* [2006] EWCA Civ 1735 at [37].
141 *Helmet Integrated Systems v Tunnard* [2006] FSR 41.
142 *Helmet Integrated Systems v Tunnard* [2006] EWCA Civ 1735 at [32].

third party or by himself. Such a duty necessarily had to be fulfilled when Mr Tunnard was working alone and outside of the office. HISL was unable to supervise Mr Tunnard in fulfilling his advisory duties and completely relied on Mr Tunnard to identify information which may be of interest to HISL and report it.[143] As a result of HISL's dependence on the unsupervised fulfilment of Mr Tunnard's advisory and reporting duty, it was contended that Mr Tunnard's contractual obligations placed him in a situation where equity imposes "rigorous duties in addition to the contractual obligations".[144]

Moses LJ accepted, with some hesitation, that because of the circumstance of his contractual obligations, if Mr Tunnard used information about competitor activity either for the benefit of someone other than HISL or for his own benefit he would be in breach of a fiduciary obligation.[145] This was because HISL had no control over, or supervision of, how Mr Tunnard used information he learned as a salesman. HISL was therefore dependent on Mr Tunnard and vulnerable to his misuse of information.[146]

However, Moses LJ was not prepared to accept that Mr Tunnard owed an obligation, fiduciary or otherwise, to inform HISL of *his own activities*.[147] This conclusion was underpinned by Moses LJ's view that HISL had not contractually restricted Mr Tunnard's freedom to prepare for departure.[148] Moses LJ emphasized that Mr Tunnard was a salesman and not a designer.[149] In the circumstances of the case, Mr Tunnard's contractual obligation to advise on competitor activity was not sufficient to take away Mr Tunnard's "pre-existing right to prepare for competition".[150] For Moses LJ, far clearer words in the contract were required "to restrict the ordinary freedom of an employee who is considering quitting his employment and setting up in competition to his own former employer".[151]

Moses LJ's reluctance to interfere with Mr Tunnard's right to engage in preparatory activities in light of the express terms of his contract has been subject to criticism.[152] Nevertheless, it is suggested that the general principles as to the incidence of fiduciary duties put forward in *Fishel* and approved by Moses LJ's in *Tunnard* are sound and consistent with the application of the fact-based legitimate entitlement test explained above. It is suggested that following a more fact-based approach would provide a solid analytical basis for New Zealand courts to determine when employees owe fiduciary duties to their employers.

143 Ibid, at [39].
144 Ibid, at [39] citing *Nottingham University v Fishel* [2000] ICR 1462 at 1491.
145 Ibid, at [44].
146 Ibid, at [45].
147 Ibid, at [46] (emphasis added).
148 Ibid, at [47] and [51].
149 Ibid, at [48].
150 Ibid, at [49].
151 Ibid, at [49].
152 See Stafford & Ritchie, above n 85, at 108-109.

The main implication of New Zealand courts adopting a more fact-based approach would be the abandonment of the idea that an employment relationship, itself, never gives rise to fiduciary duties and the recognition that fiduciary duties may potentially arise in a range of employment relationships. For a majority of employees, the incidence of fiduciary duties may still be rare. For example, for employees providing labour at an hourly rate, part-time employees or employees working on temporary basis, it is very unlikely that sufficient trust and confidence will be reposed in them to advance the best interests of his or her employer, and subjugate their own self-interest. Additionally, the existence of contractual mechanisms to dictate and constrain an employee's conduct may eliminate the prospect of fiduciary duties arising for many employees, particularly those at a "junior level".

However, when applying a fact-based approach it may be evident that some "senior" employees will owe fiduciary duties to their employers. Importantly, the imposition of fiduciary duties on such senior employees should not be seen as dependent on an employee's seniority or title. Rather, fiduciary duties are more likely to be owed by senior employees because it is more likely that such employees will have open-ended and unsupervised duties that place them in a position that require them to act in the sole interests of their employer and eschew their own self-interest. In some cases, such as when an employee is given control of an employer's property or is entrusted with securing a specific business opportunity for the employer, even relatively "junior" employees may have duties that require them to act solely in the best interests of their employer.[153] Therefore, where an employee engages in disloyal conduct in appropriate factual circumstances, a claim that an employee has breached a fiduciary obligation of loyalty may be apt. The next section briefly considers the significance of such a claim.

IV. The Significance of a Fiduciary Law Claim

A. Preparation for Competition

Because fiduciary loyalty and fidelity are similar concepts, often a claim for breach of a fiduciary duty may not add anything in substance to the claim that an employee has breached an implied duty of fidelity or an express term of the employment contract.[154] Most acts of employee disloyalty during employment, such as the taking of a business opportunity during employment, are likely to amount to a breach of an employee's duty of fidelity.[155]

However, a claim that an employee has breached a fiduciary duty of loyalty may be significant when assessing the legitimacy of an employee's preparatory activities for competition during the tenure of an employee's employment. As

153 As Fletcher Moulton LJ has explained, even an errand boy may have a fiduciary duty to account for funds entrusted to him *Re Coomber* [1911] 1 Ch 723 at 728.

154 *Lonmar Global Risks Ltd v West & Ors* [2010] EWHC 2878 (QB) at [153].

155 As in *McKay Electrical (Whangarei) Ltd v Hinton* [1996] 1 ERNZ 501 (CA).

explained above,[156] the duty of fidelity, as a general rule, does not prohibit an employee to take steps by way of preparation to compete with his or her employer.

In contrast, where an employer is able to establish that an employee owes fiduciary duties, an employer may have a greater prospect in objecting to preparatory activities on the grounds that the employee has failed to report conduct that, although not harmful to the employer, placed the employee in a position where his or her duty to the employer conflicted with his or her self-interest. Support for such an argument can be based on some English authority that suggests that a director (owing fiduciary duties to the company) must disclose his or her intention to leave the company and compete.[157]

A distinction between bringing a fiduciary and fidelity claim in the context of disclosure may be illustrated by *Rooney Earthmoving v McTague,*[158] where it was alleged that three defendants, in taking steps to set up a competing company, breached their duties as employees. One of the plaintiff's claims was that the defendants' duty of fidelity required them to disclose their intentions to set up a competing business. In the circumstances of the case, Travis J held the duty of fidelity obligated the employees to disclose conduct damaging to their employer, even where such conduct was being performed by the employees personally or where they were complicit in that conduct.[159] However, in terms of whether the duty of fidelity required the employees to disclose either their own, or a fellow employee's, intention to simply leave and compete, Travis J observed the law had not gone that far, but the position of employees who are also directors may well be different.[160] Extension of this reasoning suggests that an employee found to owe fiduciary duties may owe, as part of his or her fiduciary duty of loyalty, a duty to disclose preparatory conduct that places him or her in a position where his or her duty as employee and his or her self-interest may conflict.[161]

156 See n 59-61 and accompanying text above.

157 For a review of this authority see Peter Watts "The Transition From Director to Competitor" (2007) 123 LQR 21. In particular, see *Item Software v Fassihi* [2004] EWCA Civ 1244 and *British Midland Tool Limited v Midland International* [2003] EWHC 466 (Ch).

158 *Rooney Earthmoving Ltd v McTague* [2009] ERNZ 240 (EMC).

159 Ibid, at [141]. Compare the observations of Goddard CJ in *Nedax Systems Ltd v Waterford Security* [1994] 1 ERNZ 491 (EMC) at 500.

160 Ibid, at [142] citing the article by Watts, above n 157. Note that Travis J did find that each of the defendants breached their duty of fidelity in other respects, such as soliciting work from clients while still employed.

161 See *Hanco ATM Systems Ltd v Cashbox ATM Systems Ltd* [2007] EWHC 1599 (Ch) at [63] where it was held that an employee had a duty to disclose his own wrong doing and the intended departure of other employees. Also see *Tesco Stores Ltd v Pook* [2003] EWHC 823 (Ch) at [63] and [65] where it was observed that senior employees have a positive duty to disclose breaches of their fiduciary duty, but there is no duty on an employee to disclose breaches of contract, which do not involve a fiduciary element.

B. Jurisdiction and Remedies

A distinction between a duty of fidelity and fiduciary duties may come into focus for two further intertwined reasons. First is the issue of jurisdiction. The Employment Relations Authority has exclusive jurisdiction to make determinations about "employment relationship problems".[162] The Authority's exclusive jurisdiction includes matters related to a breach of an employment agreement,[163] and for breaches of the statutory good faith obligation.[164] As a result, a claim for breach of an employee's duty of fidelity or statutory obligation of good faith would appear to fall squarely within the Authority's exclusive jurisdiction.[165]

Claims based on breach of a fiduciary duty by an employee are less clearly within the Authority's jurisdiction. The Authority also has jurisdiction to hear:[166]

> Any other action (being an action that is not directly within the jurisdiction of the court) *arising from or related to the employment relationship* or related to the interpretation of this Act (other than an action founded on tort).

In *BDM Grange Ltd v Parker* the High Court held that the words "related to" in s 161(1)(r) had to be read in a limited way to mean any cause of action found entirely within the employment relationship itself.[167] In obiter, considering a claim for misuse of confidential information, the High Court said a claim for relief that is characterised substantially as a claim in equity will properly be within the jurisdiction of the High Court and not within the jurisdiction of the Authority.[168]

In *Transnet,* Keane J held that the High Court did have jurisdiction to hear a fiduciary claim because some of the defendants were third parties and the ability to grant a remedy against them was the decisive consideration.[169] However, Keane J's reasoning suggests that a claim solely related to the relationship between the employer and employee is within the exclusive jurisdiction of the Authority,[170] raising some doubt as to whether a claim for breach of fiduciary duty that does not involve a third party falls within the jurisdiction of the High Court. The Employment Court has subsequently considered it has jurisdiction to hear some claims in equity,[171] and claims

162 Employment Relations Act 2000, s 161.

163 Employment Relations Act 2000, s 161(1)(b).

164 Employment Relations Act 2000, s 161(1)(f).

165 But see *Eil Brigade Road Ltd v Brown* HC Christchurch CIV 2001-409-733, 5 August 2004 where the High Court decided a case involving breach of the duty of fidelity.

166 Employment Relations Act 2000, s 161(1)(r) (emphasis added).

167 *BDM Grange Ltd v Parker* [2006] 1 NZLR 353, [2005] ERNZ 343 (HC) at [66] expressing essential agreement with *Pain Management Systems (NZ) Ltd v McCallum* HC Christchurch CP 72/01, 14 August 2001.

168 Ibid, at [88]. See also at [74].

169 *Transnet NZ Ltd v Dulhunty Power* [2007] ERNZ 379 (HC) at [23].

170 Ibid, at [24].

171 See *New Zealand Fire Service Commission v Warner* [2010] NZEmpC 90, (2010) 9 NZELC 93, 633, [2010] ERNZ 290

based on breach of a fiduciary duty have been decided previously.[172] Thus, while the law in this area evolves, it may be that claims involving a breach of an employee's fiduciary duty may need to be commenced in the High Court.[173]

Second, the distinction between the duty of fidelity and a fiduciary duty of loyalty is important for remedial reasons. While some courts have warned that fiduciary law claims should not be remedy led,[174] a fiduciary law claim provides an employer with a clear remedial advantage. Damages are the primary remedy for an employee's breach of his or her duty of fidelity, and as such, will generally only compensate an employer for loss suffered. Sometimes it may be difficult for an employer to establish it has suffered loss because of an errant employee acting in competition with someone else, or on their own.

By contrast, a claim sounding in fiduciary law offers a far more preferable remedial regime in some circumstances. A fiduciary found to have breached a fiduciary duty of loyalty may be called on to disgorge his or her profits. Whether an employer has actually suffered loss is irrelevant.[175] An employer may also be awarded a constructive trust over property that represents the traceable proceeds of an employee's profits. A knowing participant in a breach of fiduciary duty may also be made liable to the employer as a result of their participation in an employee's breach.[176]

V. Conclusion

All employees owe a common law duty of fidelity to their employers. The presence of this duty can make the incidence of fiduciary duties in employment difficult to discern. This is because a fiduciary's core duty of loyalty and a duty of fidelity are similar concepts. Characterising competitive conduct of an employee as a breach of a fiduciary duty will often be unnecessary. However, in some contexts it will be advantageous for an employer to frame a claim relating to employee disloyalty under fiduciary law, particularly in light of the more generous range of remedies available.

New Zealand employment jurisprudence has been unreceptive to the notion that the employment relationship gives rise to fiduciary duties. The trend of case law has required an employee to have some other position or status to be held to owe a fiduciary duty. Non-office holding employees have

172 See *Mazengarb's Employment Law* (LexisNexis) at [ER161.5] citing *Strickett v Arthur* (1995) 4 NZELC 98,306 (EMC) (decided under the Employment Contracts Act 1991).

173 See further Michael Leggat "BDM Grange Ltd v Parker — Additional Comment" [2005] ELB 139. Compare *Aztec Packaging Ltd v Malevris* [2012] NZHC 243.

174 *Maclean v Arklow Investments Ltd* [1998] 3 NZLR 680 (CA) at 690 per Gault J. See also *Norberg v Wynrib* (1992) DLR (4th) 449 (SCC) at 481 per Sopinka J.

175 *Chirnside v Fay* [2006] NZSC 68, [2007] 1 NZLR 433 at [17]. *Stevens v Premium Real Estate* [2009] NZSC 15, [2009] 2 NZLR 384 at [32].

176 See *Consul Development Pty Ltd v DPC Estates Pty Ltd* (1975) 132 CLR 373 at 397 per Gibbs CJ. Applied in an employment context in *Timber Engineering Co Pty Ltd v Anderson* [1980] 2 NSWLR 488.

been considered to only owe a duty of fidelity to their employers. It has been contended that limiting the incidence of fiduciary duties to employee office holders may be too rigid and a tendency to focus on an employee's seniority may be unsound and misleading.

Instead, drawing weight from New Zealand Supreme Court cases examining the incidence of fiduciary obligations in commercial relationships, this article has advocated that a fact-based approach that examines when there is a legitimate entitlement for the employer to repose trust and place confidence in an employee provides a more principled approach. Reflecting the nature of fiduciary duty of loyalty, the reposing of trust and placing confidence must be directed towards an employee subjugating his or her of self-interest. Frequently, this will occur when an employee has placed himself or herself in a position where he or she must act solely in the interests of the employer. This fact-based approach is analogous to the approach taken in recent English cases, particularly *University of Nottingham v Fishel.* By applying a fact-based approach in an employment context, New Zealand courts should be more ready to recognize the incidence of the fiduciary duty of loyalty for *some* employees in respect of *some* of their duties.[177]

177 This article was accepted for publication on 7 February 2012.