immediate consideration of the Government or the draftsman;

(2) that, in relation to policy, the legislation works in the broader context so as not to disadvantage any on sectionof the community unfairly or unreasonably as against any other, and that it does not offend against the generally accepted precepts of the rule of law.

One could expand on this statement at length, but it suffices to say for the present that the efforts of members of the Committee in private practice in pursuing these objectives frequently results in legislation which some at least of their clients would be strenuously opposed to, were those clients' direct business interests taken into account. By way of example, after the Trade Practices Revision Act 1986 was enacted, the Committee pointed out to the Attorney-General that, as a result of a late amendment in the Senate, the proposed measure to close the Bowral Brickworks joint venture loophole in relation to Section 50 had been rendered ineffective. The Government moved to correct the situation in amending legislation passed in December. No doubt a number of Committee members' clients could have taken advantage of the anomaly had it remained."

Chairman Trade Practices Committee Business Law Section

The letter from Mr. Ian Tonking on the role of the Trade Practices Committee of the Business Law Section is an important statement of principle in relation to the question of the lobbying activities of organisations such as the Trade Practices Committee. It is my view that persons who act on committees such as the Trade Practices Committee do bring to bear, their perception of how relevant laws might affect the way in which the particular legal system operates including how it might affect their clients. To ignore those issues, is to (using words of Sir John Latham, in the case of *Mills v. Mills* (1978)(60 C.L.R. 150))"to live in an area of detached altruism". Members of various committees may often have to compromise a particular viewpoint in the final decision of the committee; and often these decisions of the committees are compromises which take into account various matters which relate to the issue at hand including matters not necessarily in the interests of clients.

I would welcome further comments on the question of lobbying and the role of lawyers from members of the Business Law Section and from readers of this Journal.

In this issue we feature two important articles in the ares of Intellectual Property and Company Law and the thought provoking speech of Mr. Ron Merkel Q.C. delivered at the first Business Lawyers Conference held in Sydney in October 1986. The articles, by Lindsey Naylor and Professor Bob Austin deal with interesting questions in the relevant areas. Mr Naylor discusses the scope of protection for integrated circuits which are of course so vital in our technological development whilst Bob Austin discusses a recent New Zealand case dealing with the question of the use of corporate opportunities by directors. This topic is certainly very relevant in the context of the insider trading debate.

R. Baxt

Corporate Opportunity — Directors' Conflicts of Interest After PACIFICA SHIPPING

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This paper was presented at the First Bi-Annual Business Lawyers Conference, Sydney, on 28 October 1986. Some of the ideas in it have been more fully addressed in the author's chapter, "Fiduciary Accountability for Business Opportunities", in P.D. Finn (ed.) Equity and Commercial Transactions *(Law Book Co., to be published in Autumn 1987.)*

1. Introduction

In the United States there is now a well developed "corporate opportunity" doctrine, according to which an executive director is accountable to his company for any gain arising out of a business

opportunity exploited by him but falling within his company's line of business.

Australian Courts have to date handled the "business opportunity" problem by applying to company directors the general principles of fiduciary duty. They have not yet recognised the existence of any special business opportunity doctrine. However, a version of the United States doctrine has been adopted by the Supreme Court of Canada (*Canadian Aero Services Ltd.* v *O'Malley* (1973) 40 D.L.R. (3d) 371), and in a line of New Zealand cases the most recent of which is *Pacifica Shipping Co. Ltd.* v *Anderson* (1985) 2 N.Z.C.L.C. para. 96-040. It is arguable that a version of the doctrine has also surfaced in England (*Island Export Financing Ltd.* v *Umunna,* Queens Bench Division (Hutchison J., 25 November 1985)).

The aim of this article is to note these developments and to put them into the wider context of the fiduciary and statutory duties of Australian company directors. Cumulatively, the law presents a complex mosaic of sub-rules united by some strong underlying themes, which have to do with setting appropriate standards of behaviour for executive directors of companies.

2. Liability at General Law: A Survey

In this part of the article I wish to identify the various common law doctrines which have a potential to render a company director liable to account to his company for some gain which he has made personally. I do not intend to deal with cases where the gain is made by some third party such as the director's spouse or a company in which the director is interested. Suffice it to say that the third party will be liable if he has knowingly assisted in the director's dishonest and fraudulent design, under the principles enunciated in *Consul Development Pty. Ltd.* v *DPC Estates Pty. Ltd.* (1975) 132 C.L.R. 373; and there is also potential liability for the third party under the law of bribery, the secret commissions legislation, the tort of inducing breach of contract, and various "aiding and abetting" statutory criminal offences. Nor will any attempt be made to sort out the difficult questions which arise when the director is a director of several companies, and he is prepared to account to a company for his gain but needs to know which company is to receive the benefit. As far as I am aware, Commonwealth law provides no real assistance on this issue (although the United States courts have relatively highly developed solutions) and I suspect that an Australian court would favour the company with which the particular gain has the closest factual connection, avoiding the adoption of sweeping propositions of law.

I shall speak for convenience of "directors" and "executive directors", and occasionally it will be necessary for me to distinguish between the two. Many of the propositions made about executive directors will apply to senior executives who are not directors, and some of them will extend even to more junior employees of the company. Some of the propositions will apply to "de facto" directors, who have not been properly appointed to the Board but act as such. However, I do not propose to enter into the problem of defining the word "director", beyond noting that no single definition will be adequate to identify the group of fiduciaries who are subject to each of the rules which I shall be discussing; that is to say, the various fiduciary sub-rules may well reach into the corporate hierarchy to different degrees.

I propose now to identify some areas of law which bear upon the problem of directors' accountability.

A. The Law of Breach of Confidence

A person who is not otherwise a fiduciary may become subject to a duty not to misuse information, if it was confidential information disclosed to him in circumstances which imposed on him an obligation to respect its confidential status. If the confidant is a director and the confider is his company then he will be under fiduciary constraints as well as the constraints imposed by the law of breach of confidence. Therefore, if he misuses confidential information, a company director will sometimes be liable for both a breach of confidence and a breach of fiduciary duty.

Normally a company seeking relief against a director who has misused corporate information will choose to rely on fiduciary law rather than the law of breach of confidence, because a breach will be easier to prove and the remedies are likely to be more comprehensive. Conversely, where there is doubt about the fiduciary status of the confidant (because, say, he is an employee below the level of senior executive) or there is doubt as to whether the fiduciary duty has continued after resignation, it may be preferable to rely only on breach of confidence (*Faccenda Chicken Ltd.* v *Fowler* [1985] Fleet St Reports 105).

Where the confider is not the company but the information relates to the company, a director who uses the information may find himself liable to the confider for breach of confidence and to the company for breach of fiduciary duty. The ultimate remedial consequences are difficult to predict, but the director would have no cause for optimism.

It is possible that a director who exploits for his own profit some information about his company disclosed to him in confidence by someone outside

the company, will be held liable to the confider for breach of confidence but will be held to have no liability to the company. Conversely there may be cases where the director will be liable to the company for breach of fiduciary duty but not liable to the confider for breach of confidence. This would happen, for example, where the director receives non-confidential information from a third party and uses it in a manner which puts him in a position of conflict between personal interest and duty to the company.

B. Misappropriation of Property which Belongs in Equity to the Company

It has been said that a director who takes property which "belongs in equity" to his company is a trustee of that property (see esp. *Cook* v *Deeks* [1916] 1 A.C. 554). The case law gives very little guidance as to when and why the company's equitable ownership arises. Where there is a more obvious and direct misappropriation of company property by the director, he becomes a constructive trustee of that property (*International Sales & Agencies Ltd.* v *Marcus* [1982] 3 All E.R. 551).

Cases of misappropriation of company property frequently involve other fiduciary rules. In particular, a director who takes his company's assets or facilities without authority has normally if not always put himself in a position of conflict between interest and duty. However, it seems artificial to analyse cases of misappropriation of company property in terms of other fiduciary rules such as the conflict and profit rules. It is self-evident that a director who takes his company's assets or facilities without authority has *per se* violated his duty of loyalty. Consequently, the misappropriation of property idea should be regarded as an independent fiduciary sub-rule.

The scope of the sub-rule depends upon the concepts of misappropriation and property. A workable definition of misappropriation would be that a misappropriation occurs where there is an unauthorised taking of title, possession or use with the intention on the taker's part of conferring a benefit on himself or on someone other than his principal.

The definition of the concept of property is much more difficult. In the United States, it has been held that the misappropriation of property sub-rule extends to "soft" assets like corporate information, goodwill and working time, as well as to "hard" assets like cash, facilities and contracts. In my opinion, it is undesirable to extend the concept of property to "soft" assets in this fashion. It is preferable to deal with "soft" assets problems by applying the conflict and profit rules to them as well as the business opportunity doctrine. This is because the property analysis merely adds another stage to the legal reasoning without adding enlightenment. Eventually the question has to be asked, is the particular "soft" asset in question to be treated as property for the purposes of the instant case? The answer to that question will inevitably lead us into questions of conflict of interest, the connection between the "soft" asset and the fiduciary office, and the line of business of the company. It would be simplest to go directly to these issues and not introduce the idea of property into the analysis at all. My comments are, broadly speaking, in line with Lord Upjohn's speech in *Boardman* v *Phipps* [1967] 2 A.C. 46.

Assuming that we confine the misappropriation of property idea to hard assets, it will nevertheless be very significant in that area. Sometimes the instant problem can be analysed in terms of a misappropriation by the company director of some particular asset which belongs to his company, such as a contract or some facility. Where that is the case, the ingredients of a breach of fiduciary duty are automatically established, and the only further question will be whether the company has consented to what would otherwise be a misappropriation.

C. Conflict between Interest and Duty

Before I deal with the conflict rule itself, it is necessary for me to make some remarks about the relationship between the conflict rule and the profit rule. The conflict rule requires that a fiduciary must avoid situations in which his personal interest conflicts or may possibly conflict with his duty to his principal. The profit rule provides that the fiduciary must account to his principal for any gain which he makes in connection with his fiduciary office. In both cases, the fiduciary may be exonerated by obtaining his principal's fully informed consent.

In *Chan* v *Zacharia* (1984) 154 C.L.R. 178, Deane J. explored the relationship between these rules and the rule in *Keech* v *Sandford* (1726) Sel. Cas. T. King 61. He said that *Keech* v *Sandford* is not a separate rule but is rather a set of presumptions of law and of fact used in the application of fiduciary doctrine. The conflict and profit rules were not strictly rules but should rather be seen as "themes" of fiduciary responsibility. For convenience I shall continue to refer to them as "rules", but it must be remembered that they are not to be treated like statutory propositions.

For the most part the conflict and profit rules cover the same ground and a conclusion expressed in terms of one of them can usually be re-stated in terms of the other. A fiduciary who makes an unauthorised

profit in connection with his office has usually placed his personal interest above his duty to his principal. But examples can be given where only one of the rules is attracted.

Green v *Bestobell Industries Pty. Ltd.* [1982] W.A.R. 1 is probably an example of the application of the conflict rule but not of the profit rule. In that case a manager tendered for a government contract when he knew that his company would also tender. He was held to be in breach of the conflict rule. However, since tenders were called for by public advertisement and anyone was free to respond, it could probably not be said that his profit as a successful tenderer arose in connection with his fiduciary office.

In *Boardman* v *Phipps* [1967] 2 A.C. 46 Lord Upjohn gave an example which should probably be regarded (in view of the majority decision in that case) as an illustration of the application of the profit rule but not the conflict rule. The example was of a trustee of Blackacre who, while acting as such, learns information regarding the value and sale price of Whiteacre which adjoins Blackacre. For one reason or another, the trustees cannot purchase Whiteacre for the trust. In those circumstances the trustee buys and subsequently sells Whiteacre at a profit, without any harm to Blackacre. It cannot be said that there is any real possibililty of conflict between the trustee's personal interest and his fiduciary duty, but the profit-making opportunity arose out of his office as trustee. Accordingly, he would appear to be accountable under the profit rule though not under the conflict rule.

If for no other reason than for clarity of analysis, it seems desirable to keep the profit and conflict rules conceptually separate, while recognising that their generating rationale is the same.

The conflict rule has its most obvious application to company directors, in cases where the director makes a contract with his company without its fully informed consent, and the question arises whether that contract may be set aside by the company. In that context, the application of the rule is frequently modified by provisions in articles of association which may permit the board of directors to approve a contract in which a director is interested, and sometimes even purport to allow the interested director to vote on a resolution to approve the contract (compare the more cautious approach of article 71 of Table A). Provisions of that kind are effective so long as they do not amount to an attempt to exempt an officer from or indemnify him against a liability that by law would otherwise attach to him in respect of breach of duty (see s.237 of the Companies Code). The distinction between an article which merely attenuates the director's duty and an article which invalidly attempts to exempt the director from his duty has yet to be judicially defined, though such authorities as we have suggest that s.237 will be given a broad and literal interpretation (see *Re Price Mitchell Pty. Ltd.* (1984) 2 A.C.L.C. 524 and *Papaki Pty. Ltd.* v *Scott* (1984) 2 A.C.L.C. 253).

The conflict rule has been extended to cases where the director is not a party to the contract with his company but has an interest in its performance, and to cases of conflict between duty and duty (see *Transvaal Lands Co. Ltd.* v *New Belgium (Transvaal) Land & Development Co. Ltd.* [1914] 2 Ch. 488; *Boulting* v *A.C.T.A.T.* [1963] 2 Q.B. 606). In the United States the conflict rule has also been applied to cases about the duties of a parent company to its subsidiaries.

In *Boardman* v *Phipps* the House of Lords emphasized that the possibility of a conflict between interest and duty is sufficient to render a fiduciary accountable. In his dissenting speech, Lord Upjohn said that only a "real, sensible possibility" of conflict is sufficient for fiduciary liability under the conflict rule. Subsequent Australian cases have tended to support the "real, sensible possibility" test: *Queensland Mines Ltd.* v *Hudson* (1978) 18 A.L.R. 1, 3 (P.C.); *Consul Development Pty. Ltd.* v *DPC Estates Pty. Ltd.* (1975) 132 C.L.R. 373, 399 (Gibbs J.); *Chan* v *Zacharia* (1984) 154 C.L.R. 178, 205 (Deane J.); *Hospital Products Ltd.* v *United States Surgical Corporation* (1984) 55 A.L.R. 417, 458 (Mason J., dissenting).

In cases of profit-taking by a director (whether or not the profit flows from a contract with the company) the conflict and profit rules overlap very significantly and sometimes opinions have been expressed that the conflict rule is the more fundamental one (see esp. *Consul Development Pty. Ltd.* v *DPC Estates Pty. Ltd.* (1975) 132 C.L.R. 373, 393 (Gibbs J.)). However, the conflict rule applies satisfactorily and clearly only if it is possible to identify a duty with which the fiduciary's personal interest comes into actual or potential conflict. Sometimes there will be a clear, identifiable duty, and *Cook* v *Deeks* [1916] A.C. 554 is probably a good example of such a case. In that case directors of the company made for their own benefit a profitable contract which their company was actively seeking. Clearly enough, their duty was to acquire the contract for the company, and they put themselves in the clearest possible conflict with that duty.

In other cases, however, the biggest problem about applying the conflict rule will be to determine whether the director was under any duty at all with which his personal interest might come into conflict. For example, in the *Regal (Hastings)* case [1967] 2 A.C. 134 the directors took an advantage by way of subscription for shares at a time when the company was not in a position to take the advantage for itself, and in circumstances in which it was plausible to say that they had no duty to the company at all. On facts

such as those, the crucial question is whether any duty exists; if there is a duty, it is fairly easy to say that there is a potential conflict between it and personal interest, and if there is no duty then there is obviously no possibility of conflict. The conflict rule provides no criteria for determining whether the duty exists. In these circumstances, the conflict rule must be regarded as inadequate to handle the sorts of situations which arise in the corporate area and demand legal solutions. We need to focus on the circumstances in which a duty will be imposed upon the director, and when those circumstances are identified it will probably be unnecessary to take the further step of determining whether there is a conflict between the duty and some personal interest of the director. In the corporate context, it will be enough to say that the director was under a duty to acquire the advantage for his company and failed to do so. The most sensible way to distinguish cases where the director is under a duty from cases where he is not, would seem to be to define the duty by reference to the line of business of the company. The director should be free to take a business opportunity which is outside the company's sphere of present and likely future business activities, but should be under a duty to avoid any business opportunity which falls within the company's actual or potential line of business.

D. The Profit Rule

As mentioned earlier, the profit rule requires that a fiduciary is liable to account to his principal for any gain which he makes in connection with his fiduciary office. Liability is made to depend on a test of connection or causality. The rule applies to all fiduciaries including but extending well beyond company directors. The rule extends to all kinds of collateral profits, such as secret commissions and gains produced by manipulating corporate policy (for instance as to dividends or loans) for personal advantage.

In contrast, the corporate opportunity doctrine of the United States is confined to commercial fiduciaries and deals only with the exploitation of business opportunities.

Several recent Australian cases involving commercial fiduciaries are examples of the application of the profit rule but they could not be analysed in terms of a corporate opportunity doctrine because they do not relate to the exploitation of *business* opportunities. In *Ring* v *Sutton* (1980) 5 A.C.L.R. 546 it was held that a director of a company who procured loans for himself from the company at rates not available to customers and clients of the company and less than current commercial rates, was in breach of his fiduciary duty. The Court adopted the statement of principle made by Helsham C.J. in Eq. at first instance, though it disagreed with his findings of fact. Helsham C.J. in Eq. had said (*Re Northern Rivers Finance Co. Pty. Ltd.* (1979) 4 A.C.L.R. 545, 549) that it was necessary to establish that the director's activity was so related to the affairs of the company that it can properly be said to have been done in the course of his management and in the utilisation of his opportunities and special knowledge as director. This is obviously a version of the profit rule.

In *Paul A. Davies (Australia) Pty. Limited* v *Davies* [1983] 1 N.S.W.L.R. 440 the directors of a proprietary company were held to have acted in breach of their fiduciary duty by borrowing the company's money for their own personal purposes without the consent of the shareholders. The main point of the appeal related to the question of remedies, but it is clear that the basis for fiduciary liability was the use of the directors' position in order to gain a personal advantage.

A central question about the profit rule is the question of definition of the connecting link between profit and fiduciary office. One approach to this question of linkage has been to insist on a close causal and temporal connection between profit and office. In the *Regal (Hastings)* case Lord Russell said (at 145, 147) that a director is accountable for profit arising by reason of and *in the course of* his fiduciary office. That restrictive formulation of the linkage was taken up and applied in *Peso Silver Mines* v *Cropper* (1966) 58 D.L.R. (2d) 1 and *Es-me Pty. Ltd.* v *Parker* [1982] W.A.R. 52. In the *Peso* case, it was held in effect that a director may wear two hats, and if he is approached in his private capacity he may exploit the profit-making opportunity without accounting to the company, because the opportunity has not arisen "by reason of" his fiduciary office. In the *Es-me* case, it was held that a director who had resigned from his position before taking the profit-making opportunity was not accountable, apparently because the taking of the opportunity did not occur "in the course of" his fiduciary office.

If Lord Russell's test is accepted, the profit rule is simply too narrow to deal effectively with the problem of profit-taking by company directors. The suggestion that liability can be avoided by the director simply resigning before the opportunity is taken, is obviously unacceptable. Equally, the notion that a director, even an executive director, can wear two hats and will be exonerated from responsibility if the opportunity arises when his directional homburg is no the locker-room shelf raised another prospect of avoidance and manipulation of the law.

Not surprisingly, therefore, attempts have been made to define the connecting link between profit and office more broadly. One distinguished attempt was made by Roskill J. in *Industrial Development Consultants Ltd.* v *Cooley* [1972] 1 W.L.R. 443. In that case Cooley had retired from his managing

directorship before accepting the Gas Board's contract, but Roskill J. held that he was nonetheless accountable. His reasoning (at p. 451) was that the opportunity which Cooley exploited was of "concern" and "relevance" to the company, and this degree of connection was sufficient for liability.

This "concern and relevance" test is much wider than Lord Russell's, in that an opportunity will not cease to be of concern and relevance to the company simply because the director resigns before exploiting it, and opportunities may be of equal concern and relevance to the company whether they arise on the golf course or in the boardroom.

Nevertheless, there are two disadvantages with Roskill J.'s formula. First, as a version of the profit rule it is too broad and onerous. The profit rule is intended to apply to all fiduciaries, not merely commercial fiduciaries like company directors. While a broad definition of the connecting link between profit and office seems appropriate for executive directors of companies, who are full-time professionals, it is too severe a requirement where the fiduciary is a part-time amateur undertaking his fiduciary responsibilities as a matter of goodwill — for example, an executor or trustee of a small deceased estate. For the part-time non-professional fiduciary, it seems fairer to say that he should be allowed to wear two hats, his non-fiduciary hat being a very large one, and consequently he should not be accountable for exploiting profit-making opportunities unless the connecting link between the profit and his fiduciary office is a close causal connection.

The second disadvantage with the "concern and relevance" test is that it is not particularly informative. The words "concern" and "relevance" are both vague, and it will be very hard to decide in the corporate context whether any opportunity, however remote it appears to be from the company's business, is of concern and relevance in some sense or other.

It would seem to be preferable, with respect, to adhere to Lord Russell's test, or something very like it, as a version of the profit rule, with the consequence that the profit rule is of relatively narrow operation. Commercial fiduciaries should be subjected to an additional doctrine along the lines of the corporate opportunity doctrine. Where a commercial fiduciary exploits a profit-making opportunity for his own benefit, he should be accountable to his principal for that profit whenever the opportunity was within the principal's actual or potential line of business and the principal has not given his or its fully informed consent to the exploitation of the opportunity by the commercial fiduciary.

E. The Business Opportunity Doctrine

In the United States, this doctrine is more commonly referred to as the "corporate opportunity doctrine", but it would appear to be equally appropriate whether the business structure is incorporated or organised in the form of a partnership or trust. Therefore I would prefer to use the expression "business opportunity doctrine".

Given the litigious propensities of commercial people in the United States, and the existence of 51 separate company law jurisdictions, it is not surprising that there is more than one version of the business opportunity doctrine in United States law. I have analysed the United States law, and proposals for its reform, in my chapter "Fiduciary Accountability for Business Opportunities", which will shortly be published in P.D. Finn (ed.) *Essays in Equity* (the second volume in this series). Suffice it to say here that the most common version of the U.S. law is the "line of business" test, as applied in *Guth* v *Loft, Inc.,* 23 Del. Ch. 225, 5 A.2d 503 (1939). In that case Guth was the President of Loft, Inc., a large retailer. He caused the company to cancel its order for beverages with Coca-Cola, and to buy beverages instead from Pepsi Cola, a company which he and an associate had formed. He used Loft's finance, plant, materials and employees to produce and market the Pepsi beverage, and Pepsi's main customer was Loft. Eventually Pepsi was spectacularly successful and Loft successfully brought proceedings requiring him to account for his enormous profits. It was held that because Loft's retail business involved the sale of a cola beverage, because it had a wholesale operation and because it had produced other soda syrups, it followed that the exploitation of the Pepsi formula and trade mark was within Loft's potential line of business, if not its actual line of business, and Guth should have made the opportunity available to the company.

The judgment of the Supreme Court of Canada in *Canadian Aero Services Ltd.* v *O'Malley* (1973) 40 D.L.R. (3d) 371 adopts a version of the U.S. law, but seeks to make the test as discretionary and "factor-weighted" as possible. The facts of the case were very similar to *Cook* v *Deeks*, except that the corporate executives concerned had resigned before the opportunity was exploited. They were held to be accountable. Having referred to the U.S. law, Laskin J. said that the standard of loyalty must be tested in each case by many factors, which it would reckless to attempt to enumerate exhaustively. He mentioned the factor of the position or office held, the nature of the corporate opportunity, its "specificness" and the director's relation to it, the amount of knowledge possessed, the circumstances in which it was obtained and whether it was special or even private. He expressly rejected Lord Russell's limited formulation of the connection between profit and office, at least in the commercial context, and regarded the *Peso Mines* case as supportable only on its special facts.

I would not recommend that principles be jettisoned in favour of a weighing up of factors. I do

not think it is necessary to go that far in order to break away from Lord Russell's test. It is sufficient to say that the commercial fiduciary is accountable where the opportunity arises from the principal's actual or potential line of business. It is true that the concept of "line of business" is an open-ended one. However, the concept is at least indicative of the sorts of things which should be taken into account in determining whether a director is liable. Some passages in the *Canadian Aero Services* judgment would support the adoption of the line of business test.

The *Pacifica Shipping* case is the most recent of a line of New Zealand cases which deal with questions of business opportunity. Pacifica operated a coastal shipping service. The directors announced their intention to acquire a second vessel because they had a surplus of freight. They were interested in the vessel "Seadrake". They arranged for their technical consultant, Johnston, to inspect Seadrake and other vessels in Norway. Pending a feasibility study, the board deferred final decision for a month. During that time Sands, the owner of Seadrake (on Johnston's suggestion) approached Andersen, a director of Pacifica. They formed a company (Kiwi Shipping Company Ltd.) to operate Seadrake on the New Zealand coastal service. Andersen resigned from the Pacifica board and on the same day he entered into a commitment with Sands for the charter of Seadrake. The shareholders of Kiwi Shipping Company were Andersen, Johnston and Sands. Pacifica's action was an action against Andersen for breach of fiduciary duty as director, against Johnston for breach of fiduciary duty as agent and for misapplication of confidential information, and against Sands for misapplication of confidential information acquired in the course of negotiations. The case is important because Davison C.J. reviewed the law extensively and gave support to a version of the business opportunity doctrine. He held that the case law has established the following propositions:

1. That a director of a limited company has an obligation not to profit personally from his position as director and not to allow a conflict to arise between his duty as a director and his own self interest.

2. That a director is disqualified from usurping for himself or for his own benefit a maturing business opportunity which his company is actively pursuing.

3. That the liability of a director to account for a personal profit made from the use of an opportunity available to him because of his fiduciary relationship with the company does not depend on fraud, or absence of bona fides. The liability arises from the mere fact of a profit having been made.

4. A director's liability to account is not unlimited. It is a defence available to a person in such a fiduciary capacity that he made profits with the informed consent of his principal.

5. Deferment of a company's plans does not entitle a director to usurp those plans or business opportunities flowing from them.

Applying these principles, he held that Andersen had usurped a business opportunity of his company.

The *Pacifica* case, and earlier New Zealand cases which are discussed in Davison C.J.'s judgment, raise the question of whether it is necessary for liability that the business opportunity be specifically and closely identified. In *CBA Finance Holdings Ltd.* v *Hawkins* (High Court Auckland, unreported, 2 April 1984). Barker J. held that the principle of the *Canadian Aero Services* case did not extend to a global business opportunity where the defendant merely wished to take advantage generally of the course of business being pursued by the plaintiff as distinct from a particular business or market opportunity under consideration by the plaintiff company. In that case Mr. Hawkins had set up a finance company which was a rival to the plaintiff. His activity involved planning, approach and perception of the market opportunity while he was an executive director of CBA Finance. Barker J. refused to extend the *Canadian Aero Services* case to that situation.

In *Pacifica*, Davison C.J. agreed with Barker J.'s analysis in *CBA Finance*, but he held that on the facts of the instant case the business opportunity involved a specific project, namely the introduction of a second vessel on a particular route, and as such it was not merely a global opportunity of the kind referred to in the *CBA Finance* case.

The New Zealand cases also specifically address the effect of resignation. In the *Pacifica* case Davison C.J. supported the statement of principle made by Barker J. in the *CBA Finance* case. Barker J. said:

"In general terms the cases show that an employee has a continuing fiduciary duty extending after the date of termination of his employment in the following kinds of situation:

(a) where the employee is using or seeking to use the employers' confidential information;

(b) where the employee is actively canvassing customers of his former employer and/or using lists of customers and the like;

(c) where the employee has during his former employment set up some business transaction or engineered some advantage which he then proceeds to use for his own end after he has left the employ of the employer."

The facts of *Island Export Financing Ltd.* v *Umunna* (Queens Bench Division, unreported, 25 November, 1985) were generally similar to the facts of the *Canadian Aero Services* case. Hutchison J. accepted a version of the corporate opportunity doctrine and cited the *Canadian Aero Services* case. He expressly rejected a submission that there is no continuing fiduciary duty after termination of employment.

The case is interesting on the question of the

effect of resignation. In the *Canadian Aero Services* case, Laskin J. had said that a director is precluded from usurping a corporate opportunity even after his resignation, "where 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, or where it was his position with the company rather than a fresh initiative that led him to the opportunity which he later acquired" (at p.381). In the *Island Export* case, Hutchison J. disagreed with the last part of this formulation. He said that it would be wrong to hold directors accountable "whenever they exploit for their own or a new employer's benefit information which, while they may have come by it solely because of their position as directors of the company, in truth forms part of their general fund of knowledge and their stock-in-trade."

The net effect of all of this is:

(a) that it is plausible to contend that there should be an additional fiduciary doctrine, over and above the law of breach of confidence, the misappropriation of property rule, the conflict rule and the profit rule, to render a commercial fiduciary accountable for the exploitation of a business opportunity falling within his principal's actual or potential line of business;

(b) there is now a developing body of Commonwealth authority to support the proposition that such a principle exists.

Over the next few years, we can expect to see the business opportunity doctrine confirmed in cases in this country and in other parts of the Commonwealth. Recognising the existence of the doctrine is merely the beginning of this branch of legal development, for it will be necessary to develop a body of precedents which will clarify its scope and operation. Apart from a need for precedents on the central idea of actual or potential line of business, we shall need to have some further judicial guidance on the extent of liability after resignation, on the extent to which the doctrine should be applied to others than full-time executive directors (such as executive employees and non-executive directors), and on the extent to which the doctrine will apply where the corporation is not actively seeking the opportunity for itself or perhaps is unable to take the opportunity for financial or other reasons. On this last issue, it is established in Commonwealth law (though the authorities in the United States are inconsistent) that the conflict and profit rules render a fiduciary accountable for profits even where his principal is unable to take the profits because of some legal or financial impediment (*Boardman* v *Phipps* and the *Regal (Hastings)* case are the main authorities). There is surely no good reason for treating the business opportunity doctrine any differently, and consequently the reference in the *Canadian Aero Services* and *Pacifica* cases to opportunities which the corporation is "actively pursuing" should not be regarded as identifying a limitation to be imposed upon the doctrine.

F. Waiver and Exoneration

This is a large topic, and for some reason is the single aspect of the case law which has attracted extensive attention in Australian law journals. It is a characteristic of the conflict and profit rules, and should be a characteristic as well of the business opportunity doctrine, that the principal can exonerate the fiduciary from what would otherwise be a breach of duty by giving his fully informed consent to the fiduciary's activity, and the principal may also waive a breach after it has been committed provided once again that he is fully informed.

Where the principal is an individual, the application of these propositions is relatively straightforward. A difficulty arises, however, where the fiduciary is a director and the person to whom he owes his fiduciary duties is the company which he directs. The question in that context is: which corporate organ should be allowed to exercise the principal's rights of waiver and exoneration?

Commonwealth case law has led us into an appalling muddle. There is inconsistency on the questions:

(i) whether it is admissible to exonerate a director from breach of his fiduciary duties (contrast *Cook* v *Deeks* [1916] 1 A.C. 554 on the one hand with *Furs Ltd.* v *Tomkies* (1936) 54 C.L.R. 583, the *Regal (Hastings)* case [1967] 2 A.C. 134 and *Queensland Mines Ltd.* v *Hudson* (1978) 18 A.L.R. 1; and note the suggested reconciliation in *Prudential Assurance Co. Ltd.* v *Newman Industries Ltd.* (No. 2) [1980] 2 All E.R. 841 per Vinelott J.);

(ii) whether (if so) the Board of Directors can ever be the assenting organ (compare *Furs Ltd.* v *Tomkies* and the *Regal (Hastings)* case);

(iii) whether (if consent by the shareholders is possible) it must be expressed unanimously or by ordinary resolution (again, compare *Cook* v *Deeks* with the other cases cited above);

(iv) whether interested directors should be excluded from voting as shareholders (compare the *Prudential* case with *North West Transportation Co.* v *Beatty* (1887) 12 App. Cas. 589).

I do not propose to contribute to the confusion by saying anything more about it on this occasion.

3. Liability Under Statutory Law

A comprehensive list of the statutory provisions which may be relevant where a director acts in a disloyal and self-interested way would be a very long one. Regard would have to be taken, inter alia, of the Crimes Act, the Secret Commissions Prohibition Act and the Securities Industry Code, as well as the Companies Code. Even if we confine our attention to

the Companies Code, it is striking that there is a range of disuniform provisions to be taken into account: ss.228, 229, 230, 233, 556 and the accounts provisions and the Seventh Schedule are amongst the provisions which have particular relevance. It seems to me that many of these provisions are addressing similar problems in markedly different ways. There is no uniformity on such questions as the extent to which breach of duty should attract onerous criminal penalties, whether offences should be defined in terms of absolute liability or a high degree of mens rea, and whether the statutory provision can be avoided by shareholder waiver or exoneration. I am on record as saying that the statutory law of directors duties is in need of a thorough overhaul, to try to make uniform the principles and approach which should be taken to statutory re-enforcement of the general law.

There is no time here to give an exhaustive review of the statutory provisions. Our focus today is on the conflict/profit/business opportunity area rather than on the director's duty of care, skill and diligence and his duty to act bona fide for the benefit of the company. The statutory provisions extend to these other matters and a full review would need to look at them as well.

The Sections which are most relevant to the case law which I have discussed above, are ss.228 and 229.

Section 228(1) deals with disclosure of interests in contracts. As pointed out above, the Articles of the company will frequently set a standard of disclosure which is lower than the general law would otherwise require. While, therefore, s.228(8) preserves the general law in addition to the Section, the effect of the Articles will frequently be to make the general law relatively insignificant, and the main emphasis will therefore be to comply with s.228 by disclosure to the directors either in particular or in general terms.

Several other provisions are approximations of the general law (which is preserved) but an apparent failure on the part of the draftsman of the legislation to understand the scope of the general law has led him to impose some curious and almost whimsical restrictions in the wording of the Sections. For example s.228(5), which is evidently intended to deal generally with conflicts of interest, applies only where the director holds an office or possesses property whereby a conflict is created. Conflicts which arise in other circumstances are evidently not covered. Section 229(3) applies only when the officer "make[s] improper use of information acquired by virtue of his position as such an officer". Proof of this offence seems to involve showing that the information was actually made use of; the sub-Section applies only to "information" and the connection between profit and office is defined in very limited terms. Much the same points can be made about s.229(4), which speaks in terms of making "improper use of his position as such an officer". *Waldron* v *Green* (1978) C.C.H. C.L.C. para. 40-381 confirms that these provisions are likely to receive a restrictive interpretation.

Neither s.229(3) nor s.229(4) covers the range of situations which may fall within the profit rule. Neither of them is expressed in terms which are apt to re-enforce the business opportunity doctrine. Therefore in a significant range of situations, Sections 228 and 229 will be irrelevant. Even where they do apply, their interpretation is likely to be governed by the cases of the general law.

The Lawyer as Client

Address by Ronald Merkel Q.C. to Business Lawyers Conference at Sydney on Monday 27th October, 1986.

1. The Problem

The role of the lawyer as a professional adviser has recently come under greater scrutiny than ever before. At the present time several Solicitors and Accountants and one member of Queen's Counsel have been charged by the Director of Public Prosecutions in relation to tax offences. One may expect that other advisers may be charged. It is too narrow a view for the profession to see the issues raised as limited to tax conspiracies. As the challenge of law enforcement extends to other regulatory bodies who are charged with prosecutions under their legislation one can readily see problems and issues arising in other commercial areas similar to those recently experienced in the tax area. Such bodies as the NCSC and the TPC as well as the respective officers charged with Customs prosecutions may well find that the line between wrong or misconceived advice and criminal advice is increasingly difficult to draw.

2. It is of course no coincidence that these problems are occurring in a climate —

(a) where the legal profession has become involved in a participatory sense in many of the commercial events in respect of which they are required to give advice.

(b) where the standing of the legal profession has been seriously eroded by continuing large trust defalcations.

(c) where the profession has had an active involvement in the tax avoidance industry.

(d) where charges have been brought against some members of the judiciary.