# THE LIABILITY OF INNOCENT THIRD PARTIES IMPLICATED IN ANOTHER'S BREACH OF CONFIDENCE

By
JENNIFER STUCKEY*

*The courts have yet to decide definitively how the competing equities of the wronged discloser and the innocent third party, both of whom have been taken unfair advantage of by the misbehaving confidant, are to be balanced in terms of equitable remedy. The writer argues, first, that the defence of bona fide purchase for value without notice is an inappropriate one for the third party to invoke in an action which is not concerned with property rights, and suggests the adoption of the more flexible defence of change of circumstances. Secondly, the writer discusses at what point an innocent third party should be held to have become liable to the discloser: when he becomes aware of the confidant's breach of duty or when he first has the confidence disclosed to him by the misbehaving confidant?*

The action for breach of confidence is concerned with the obligations enforced in Equity, which arise out of or attach to a special relationship of trust between discloser and confidant. For the discloser to have an action *in personam* against a third party, who had obtained the confidential information, but with whom he had no direct relationship of trust or confidence, that third party must somehow be implicated in the confidant's breach of duty. Then the obligation which attaches to the confidential relationship, between discloser and confidant, might also be said to bind the conscience of the third party indirectly.[1] It is not enough that the third party has merely obtained the information. A party who discovers, for example, the particular trade secret in question by the independent and lawful processes of reverse engineering,[2] or independent rediscovery; or who merely finds or comes across the information quite by accident — for example, in an abandoned notebook,[3] — has not brought himself into any relationship with the discloser, either directly or indirectly, through implication in any confidant's breach of duty. The third party who has obtained the information by what Professor Jones describes as 'reprehensible means', may provide an exception to this general principle:

> It would be rash, however, to conclude that the stranger who sells information obtained, for example, from the use of electronic bugs cannot be enjoined and is not liable to make any recompense or account for his profits to the plaintiff. Equity, to borrow a metaphor, should not be past the age of child-bearing. A defendant who has taken good care not to enter any relationship of any sort

*B.A., LL.B.(A.N.U.), LL.B.(Cambridge).

> with the plaintiff and who has obtained confidential information by reprehensible means should be in no better position than a defendant who is given and deliberately breaches the plaintiff's confidence.[4]

It seems that this view has been judicially accepted, at least in the situation where it is regal privacy which is infringed by electronic bugging. In May 1981 a journalist claimed to have received from Australian republicans tapes of telephone conversations between Prince Charles and Lady Diana Spencer and, between Prince Charles and the Queen. Temporary injunctions were granted by Bingham J. to restrain the publication of the contents of those tapes the authenticity of which was in any case seriously in doubt.[5]

However, the position generally with regard to the liability of dishonest third parties is settled. Because Equity will impose obligations only where a relationship of confidence exists between the parties, the issue of fact as to whether the third party has been fixed with knowledge of the confidant's breach of duty is crucial in deciding the liability of such a third party. If the third party had knowledge from the outset of the events which constituted the breach of confidence, he will be completely implicated in the confidant's dishonest conduct, and relief will be granted to the plaintiff against the third party.[6]

The position with regard to the liability of innocent third parties, on the other hand, is far from settled. The courts have yet to decide definitively how the competing equities of the wronged discloser and the innocent third party, both of whom have been taken unfair advantage of by the misbehaving confidant, are to be balanced in terms of compensation. Two questions which relate directly to the liability of an innocent third party to compensate the discloser will be discussed in this article. First, the defences, if any, which are available to such a third party. Secondly, the point at which the innocent third party will be held to have become implicated and so liable to the discloser; that is, either when he becomes aware of the confidant's breach of duty or, when he first has the confidential information disclosed to him by the misbehaving confidant.

## I. POSSIBLE DEFENCES AVAILABLE TO AN INNOCENT THIRD PARTY

There are three main schools of thought on this issue.[7] The first denies that the innocent third party has any equity to be balanced against that of the discloser. It would impose a strict liability upon the innocent third party. Adherents of this school also support the view, discussed below,[8] that the duty of confidence is a sufficiently stringent one to hold an innocent third party implicated from the moment he acquires the confidential information. The duty is absolute and, it is argued, the liability also. The discloser will always be entitled to relief against the defenceless third party. No consideration will be given by the Court to the equities which might be claimed to exist between the two innocent parties, since the equity of the discloser is absolute and pre-eminent. However, as Dr Finn has observed, such an absolute liability will be unattractive to the courts as a solution because:

> [I]t pays no regard to the manner in which the information was acquired by the third person, for example, whether he purchased it without knowledge of the

> breach of the duty. Neither does it look to any detriment which may be suffered by him, if, in the circumstances, he is enjoined from continuing to use it.[9]

The other two schools postulate alternative defences for innocent third parties. The first supports the utilisation of the defence of bona fide purchase without notice;[10] the second proposes the defence of change of circumstances to the third party's detriment.[11]

1. *The Defence of Bona Fide Purchase for Value Without Notice*

It has been argued that a third party, who received information from a confidant, in breach of that confidant's duty to his discloser, may be relieved of all liability if he takes the information as a bona fide purchaser for value without notice, that is, in reasonable ignorance of the breach of duty by the confidant.[12] This defence would only be available if the action for breach of confidence enforced a proprietorial right in information. However, the action for breach of confidence enforces in Equity's exclusive jurisdiction a broadly-defined duty of good faith arising out of a proven relationship of trust or confidence; it does not enforce or recognise legal or equitable property rights in the information transmitted within that relationship. The present writer has suggested elsewhere that the analogy of information with property may be usefully employed for the strictly circumscribed purpose of delineating principles upon which compensation may be assessed for breach of confidence. However, she has also suggested that there is no further use to which the analogy of information with property can be put, in regard to the action, without creating unnecessary confusions of principle.[13] In addition Professor Gareth Jones has doubted:

> whether the mere payment of money should, in itself, defeat a restitutionary claim whose essence is a duty of good faith, a duty not to take unfair advantage of the plaintiff's confidence.[14]

This doubt is strengthened by the situation which could arise in the case of a breach of personal confidence: should the mere fact that the third party paid money for the information, without notice of the breach, allow him to go ahead and publish such information, thus inflicting disproportionate personal suffering on the discloser? While the discloser may well be able to proceed against his confidant, this will provide no genuine relief against the real harm which could be done to him by the 'bona fide purchaser'.

It is this situation also which distinguishes the duty of the confidant from that of the trustee; and which reveals the inadequacy of any analogy of information with trust property in a consideration of the relevance of the bona fide purchase defence to the action for breach of confidence. Both the beneficiary and the discloser have *iura in personam* to enforce certain equitable obligations arising out of specific relationships of trust between them and the defendants. The benefit of the obligation is, in the first situation of trust, title to specific property which is the subject matter of the trust; whereas in the breach of confidence situation, it is simply a right to restrain the use of certain information, which does not in itself involve any title to property at all.

While the defence of bona fide purchase has been accepted in actions for breach of confidence in the United States,[15] it has never been unequivocally accepted in England or Australia. It seems to have been argued in three cases central to the early

development of the action, where injunctions were granted against third parties.[16] Although the defence was adverted to with approval in *Morison* v. *Moat,*[17] it was not upheld in any of those cases. In *Prince Albert* v. *Strange*[18] value was given and, although the defendant denied that he had knowledge the court imputed constructive notice to him. In *Abernethy* v. *Hutchinson*[19] constructive notice was again imputed to the defendants although, it was arguable on the facts whether value had been given and whether the third parties had knowledge of the breach. However in *Morison* v. *Moat,*[20] where it was held on the facts that the third party was a volunteer, Turner V.C. did accept that this defence could be invoked:

> It might indeed be different if the Defendant was a purchaser for value of the secret without notice of any obligation affecting it; and the Defendant's cause was attempted to be put on this ground... but I do not think that this view of the case can avail him, for, in whatever character he may stand as appointee, he has no consequential right in the secret. So far as the secret is concerned, he is a mere volunteer deriving under a breach of trust or of contract.[21]

Similarly, there have been more recent cases in which, although the third party has been held to be a volunteer, judicial dicta have adverted to the possible use of the defence of bona fide purchase.[22] In *Printers and Finishers Ltd* v. *Holloway*[23] Cross J. said:

> If authority is needed for the grant of an injunction against someone who has acquired — or may have acquired — information to which he is not entitled without notice of any breach of duty on the part of the man who imparted it to him *but who cannot claim to be a purchaser for value,* I think that it can be found in the case of *Prince Albert* v. *Strange* (emphasis added).[24]

And in *International Tools Ltd* v. *Kollar,*[25] Kelly J.A. said:

> If it had been established that he (the defendant) was an innocent purchaser from the co-defendants for value without notice he might be in a position where he could successfully resist the plaintiff's claim for an injunction...[26]

Both cases arose out of similar fact situations where an employee of one firm left that employment to join a rival firm, taking with him trade secrets of his former employer. In each case, notice of such breach of the ex-employee's duty was an issue of fact. It seems that it was consistently assumed that the offer of new employment in each case was not 'value' given by the third party, the rival firm, and so the defence failed.

The only English decision to deal with the defence of bona fide purchase in any depth is *Stevenson, Jordan & Harrison Ltd* v. *MacDonald & Evans.*[27] The issue was whether an injunction could be granted to restrain a publishing house from publishing a book alleged to contain confidential information which, it was learnt after the contract with the author/confidant was made, but before publication, was given in breach of confidence. The defendant publishers argued that by reason of their bona fide acquisition without notice of the right to publish, the fact that such a publication would disclose the plaintiff company's confidential information was no ground for the grant of an injunction. Lloyd-Jacobs J. at first instance rejected this argument:

> Does this circumstance frank their avowed intention to consummate Mr Hemming's (the confidant's) wrongdoing? The original and independent

> jurisdiction of this Court to prevent, by the grant of an injunction, any person availing himself of a title which arises out of a violation of a right or a breach of confidence, is so well established as a cardinal principle that only a binding authority to the contrary should prevent its application by this Court... The wrong to be restrained is not the entry into the contract to publish, but the act of publishing, and an innocent mind at the time of the former cannot overcome the consequences of full knowledge at or before the time of the latter.[28]

Perhaps the most interesting part of the judgment is the cryptic consideration of Turner V.C.'s comment in *Morison* v. *Moat*[29] on the availability of the defence of bona fide purchase. He comments that, "Such a view is not inconsistent with the power of the court to prevent disclosure by injunction if proceedings are commenced in time"[30]; that is, presumably before any harm is done to the discloser. His Honour seems to be of the opinion that, while the bona fide defence may apply in situations where harmful consequences have already been suffered by the discloser, as a result of the confidant's breach of duty, it has no application in situations where, as in the instant case, injunctive relief could prevent any harm being suffered by the discloser at all.

The authority of Lloyd-Jacobs J.'s judgment is questionable, and it has been observed that it may be doubtful whether the facts of the case supported his assumption that the publishers had actually given value for the information.[31] In addition, the appeal from his decision was upheld on the ground that the information in question did not possess the necessary quality of confidentiality. Nevertheless, although there was no need to decide the issue of the bona fide purchase defence, Lord Evershed M.R. did support Lloyd-Jacobs J.'s view:

> indeed, it would be, to my mind somewhat shocking if reputable publishers, who discovered that there was in some work which they had acquired a gross breach of faith, publication of which would involve the ruin of some business, yet nevertheless could say, having discovered that fact before they had published or incurred any substantial expense, that they were entitled to go on with their publication. The learned Judge thought that the arm of the law was not too short to restrain such conduct.[32]

It is suggested therefore, that the defence of bona fide purchase is not appropriate in the action for breach of confidence for two reasons. First, and fundamentally, because its theoretical availability is premised upon the inaccurate analysis of the action as one which enforces property rights in information. Secondly, because of the possibly inequitable consequences of its utilisation, the defence may license a use of the information which could inflict disproportionate harm upon the discloser.

2. *The Change of Circumstances Defence*

This more flexible defence, which has been proposed by Professor Gareth Jones as an alternative to that of bona fide purchase, avoids the difficulties already discussed.

> A good-faith defendant who is later told that information has been given to him in breach of confidence should be excused from liability if he has irrevocably changed his position to his detriment, so that it would be inequitable to grant the plaintiff any relief.[33]

He cites with approval the United States Restatement of Torts which outlines the steps that a third party may have taken which will give rise to the defence.[34]

> The issue is whether the imposition of the duty would be equitable under the circumstances. Thus, if the recipient makes a substantial investment in plant and machinery for the use of the secret, that may be a sufficient change of position. Or, if he liquidates another business in order to establish a new business on the basis of the secret, that may be a sufficient change of position even before the new business is established. Again, if he makes substantial expenditures in surveys and research preparatory to establishing the business or in an effort to improve the secret process, he may thus change his position sufficiently. On the other hand, if he merely makes up his mind to do something in the future and carries on negotiations with others, he is not undergoing a change of position sufficient to relieve him from liability.[35]

He stresses that in each case it will be a question of fact whether the third party's change of position is sufficiently detrimental to relieve him of liability.[36] The present writer would also add the requirement that the detriment to the third party must in all respects outweigh the detriment, or prejudice, caused to the plaintiff. This consideration will be of particular importance in cases involving personal confidence.

Professor Jones also acknowledges the difficulty which third parties will face in establishing that the change of position has been irrevocable; but he asserts that it is only equitable that "any change of position, even if it is not irrevocable, may persuade the court to limit the character and quality of the plaintiff's remedies".[37] If the change of position is not held to be totally irrevocable, it may be thought sufficient, for considerations of fairness, to dictate that the plaintiff be satisfied with compensation, instead of an injunction and an account of profits. The advantages of this defence have been summarised in this way:

> 1. it gives a measure of protection to both innocent parties — to the third party where he cannot be restored easily to his initial position, and to the discloser where the injury to him can be avoided by paying to the third party his expenditure for the information;
>
> 2. it avoids bringing yet another misleading analogy, the bona fide purchaser, into confidence law; and
>
> 3. it possesses a flexibility not possessed by either of the two views previously discussed[38] (i.e. the first school imposing an absolute duty and that which proposes the defence of bona fide purchase).

Those who consider that the bona fide purchase defence is the most appropriate have voiced two main objections to the 'change of circumstances' defence. The first objection is that such a defence would undermine commercial certainty; the second, that inventors would be discouraged from utilising the patent system and the superior protection which it offers.

First, it has been argued that:

> Commercial certainty would be seriously undermined if a bona fide purchaser of information were to take subject to the risk that it might subsequently emerge that the information was confidential, and that the purchaser might be obliged to forego the benefits of what he had paid for in good faith. In addition, as between the innocent plaintiff and the innocent defendant it is arguable that the plaintiff is more to blame for what has transpired.[39]

Further, it is argued that the plaintiff could have patented his invention if possible, protected himself by express contract or, have been more circumspect in his discussions with the confidant.[40]

The obvious first response to this argument is that if both parties are 'innocent', inasmuch as they both acted honestly and in good faith, it is questionable how, in an equitable sense, one can be 'more to blame' than the other. Secondly, the action for breach of confidence is designed to protect a discloser in the situation where he has no other legal protection for his secret. Equity considers that certain obligations of good faith ought to arise out of the special relationship created between the confidant and discloser in that situation. Thirdly, and perhaps most fundamentally, there are situations in which it is suggested Equity should recognise that 'commercial certainty' (that cherished policy always pursued at common law) should be sacrificed to other considerations: in particular situations in which personal confidence has been breached.[41] The theory behind the second objection to the 'change of circumstances' defence has been explained by W. R. Cornish, although not specifically in the context of this particular debate:

> It can be argued that in cases where the law offers the industrial researcher a choice of protection for an inventive idea under one or other of these regimes, he should be induced to prefer obtaining a patent (with its advantages of giving publicity to the idea) by making more substantial remedies available to him for patent infringement than for breach of confidence.[42]

The critics of the 'change of circumstances' defence argue conversely that if the defence of bona fide purchase is not available to an innocent third party:

> the incentive on the part of persons in the community of an inventive disposition to make use of our developed system of patent law would be greatly diminished. This would mean that secret information about useful techniques would remain secret, a result manifestly not in the interests of society.[43]

The writer finds it difficult to understand the relevance of whatever small overlap with patent jurisdiction there may be to the action for breach of confidence as a whole. The equitable action for breach of confidence is concerned with patentable and unpatentable information; it is never concerned with information which already has the statutory protection of a patent.[44] Patent protection provides a much wider protection for the invention: as a common law chose-in-action it is not dependant upon any special relationship which must be established to invoke the aid of Equity in a breach of confidence suit. The actions are complementary to a small extent, in that the action for breach of confidence may be invoked to protect information which, while patentable, has not actually been patented. However, the actions are quite distinct in terms of the rights which they enforce and, in terms of the kinds of legal protection they offer to the disclosers of secret information. Therefore, it is difficult to accept the argument that the availability of the more flexible defence of 'change of circumstances' could have the purported effect of discouraging inventors from patenting their inventions. It may be said that the objections to this defence are not fundamental and that the defence allows for a more delicate and sensitive balancing of the equities of discloser and innocent third party, where it has been demonstrated that no restitutionary proprietary claim ought to be available.

## II. WHEN, IF AT ALL, DOES A THIRD PARTY INNOCENTLY IMPLICATED IN ANOTHER'S BREACH OF CONFIDENCE BECOME LIABLE TO THE DISCLOSER?

This question cannot be answered without an analysis of the nature of the equitable duty of confidence itself. Without such an analysis of the obligation the confidant owes to the discloser, no conclusions can be drawn about the nature of any derivative obligation which an innocent third party implicated in the confidant's breach might owe. Such a third party's obligation is properly described as derivative and not primary. There are two competing judicial formulations of the duty. Lord Greene M.R. in *Saltman Engineering Co. Ltd* v. *Campbell* defined the confidant's obligation in this way:

> If a defendant is proved to have used confidential information, directly or indirectly obtained from a plaintiff, without the consent, express or implied, of the plaintiff, he will be guilty of an infringement of the plaintiff's rights.[45]

Alternatively, Lord Denning M.R. in *Seager* v. *Copydex (No.1)* has proposed this definition:

> he who has received information shall not take unfair advantage of it. He must not use it to the prejudice of him who gave it without obtaining his consent.[46]

The better formulation is that of Lord Greene M.R.[47] So defined, the duty is a strict one: it is "a duty not to use the information without the discloser's consent".[48]

Recent academic writing has shown that there can be no doubt that the duty of confidence is a fiduciary obligation[49] and current judicial opinion seems to accept this view. Lord Shaw's comments in *Schering Chemicals Ltd* v. *Falkman Ltd* are confined to the commercial context:

> the communication in a commercial context of information which at the time is regarded by the giver and recognised by the recipient as confidential, and the nature of which has a material connection with the commercial interests of the party confiding that information, imposes on the recipient a fiduciary obligation to maintain that confidence thereafter unless the giver consents to relax it.[50]

There is no reason in principle why the duty to respect personal confidence should not be considered similarly fiduciary. It is the writer's view that the definition of Lord Greene M.R. is the correct one. He defines the duty as strictly imposed upon a confidant not to disclose the information transmitted within the confidential relationship of trust without the discloser's consent. The confidant must therefore be classified as a fiduciary, which simply means that his behaviour is governed by equitable rules analogous to those rules which govern the behaviour of other fiduciaries. It is this conclusion upon which the following analysis depends.

No doubt, there are situations in which an innocent third party will become implicated in a confidant's breach of duty. In such cases a balancing of the competing equities of the wronged discloser and the innocent third party will indicate that the discloser should be entitled to redress against the third party, either in the form of injunctive and/or compensatory relief. The difficulty lies in formulating the legal principles whereby these equities are to be balanced properly.

There are two views, as to when the conscience of an innocent third party becomes bound in Equity through implication in the confidant's breach of duty, which are

based upon the alternative definitions of the duty. The most influential view is that his conscience will only be bound from the time when he acquired knowledge of the breach of duty by the misbehaving confidant:

> (The defendant) will then realise that, if he continues to act as he has been acting, he may take unfair advantage of the plaintiff. The application of the equitable principle of good faith demands, in my view, that the defendant's liability to make restitution to the plaintiff should arise when he knows or ought to have known that he is breaching confidence. From the moment he acquires that knowledge (but not before) he should be under an equitable duty to the plaintiff.[51]

The alternative view is one based upon what is arguably the best judicial formulation of the duty itself, that of Lord Greene M.R. in *Saltman Engineering Co.* v. *Campbell Engineering Co.*[52]

It is the discloser's lack of consent to the use, not the confidant's motives or whether he consciously intended such a consequence,[53] which is the crucial factual consideration in finding a breach of duty by the confidant. It may be that Lord Greene's formulation of the duty is an obligation strict enough to extend to an innocent third party even before he is aware that the secret has been divulged to him by the confidant in breach of his duty.[54] On this view, considerations of the third party's honesty, his state of actual and constructive knowledge of the breach and the general reasonableness of his behaviour in the circumstances would be considered highly relevant when the court is assessing the appropriate remedies to be awarded against him[55] but, irrelevant to his initial liability. This initial liability arises immediately by virtue of his consequential implication in the confidant's breach of duty and the binding of his conscience in Equity from the very moment he obtains the information indirectly from the plaintiff.

Professor Jones argues in terms of Lord Denning's alternative formulation of the duty.[56] He asks how an innocent third party can be said to have taken unfair advantage of the plaintiff if he was unaware that the information was given to him in a breach of confidence or, was unaware even of the existence of the plaintiff? Can it be equitable for the third party's conscience to be bound if the third party was wholly and justifiably ignorant of any wrongdoing?

It has been pointed out that such considerations have regularly been excluded by courts of Equity in the context of unknowing breaches of fiduciary obligations generally:

> [T]he courts have recognised the harshness of punishing a fiduciary who unknowingly breaches a duty of good faith, yet the courts have often observed that such duties can only be effectively maintained if the guilty and innocent alike are punished for transgressing the requirements of a particular duty.[57]

This classical rationale justifying the strict standards Equity exacts from fiduciaries is not immediately relevant to the issue of the liability of a third party: such a third party cannot be characterized as a fiduciary. The third party has never been brought directly into one of those special relationships of trust which Equity fiercely protects. It is the confidant upon whom such a duty of trust is imposed. The third party's liability to the discloser only arises through consequential implication in the confidant's breach of duty. The crucial issue is: at what point can the third party be

said to be implicated in that breach so that his independent, though derivative, liability arises.

The answer in terms of the strict interpretation of the duty is this: if the confidant's primary duty is breached, regardless of whether the confidant's wrongdoing was conscious or not, as the courts have held in *Seager* v. *Copydex (No.1)* and *Talbot* v. *General Television Corp. Pty Ltd,*[58] then that duty is strict enough to impose a liability upon any third party who does the same. So, the classical rationale applies: the duty is paramount. The implication of the third party by his actions in the breach of the primary duty of the confidant founds his independent but derivative liability. However, unlike the dishonest third party who was always aware of the wrongdoing, the innocent third party should be treated leniently in terms of remedies to be awarded against him. He has only been implicated by circumstance, not by his own design. He is an "innocent... punished for transgressing the requirements of a particular duty"[59] and Equity should take a flexible view of his predicament. Considerations of his honesty, his state of actual and constructive knowledge of the breach and the reasonableness of his behaviour in the circumstances should be taken into account when the court is determining whether the plaintiff could demand an injunction and/or an account of profits or merely monetary compensation against him. In such circumstances, the proposed defence of change of circumstances should also be available to the innocent third party who has radically changed his position. If the change of circumstances defence is not adopted by the Australian courts this strict view leaves open the technical possibility that an innocent third party may have to account to a discloser for all profits made in unknowing breach of confidence. This appears too rigid to be acceptable.

If, on the other hand, Professor Jones' view is accepted, interesting questions then arise as to the *kind* of knowledge which the innocent third party must acquire for his conscience to be bound. Professor Jones argues that "knowledge and good faith should be interpreted to embrace constructive and imputed knowledge"[60] on the ground that:

> A defendant who acts unreasonably in thinking that he is not breaching the plaintiff's confidence has surely taken unfair advantage of the plaintiff.[61]

This line of reasoning was followed by the courts in *Seager* v. *Copydex (No.1)*[62] a case which did not involve third party liability, and *Talbot* v. *General Television Corp. Pty Ltd*[63] a case which did. Both cases show that fact situations can arise where the courts will hold the confidant liable for breach of confidence through mere inadvertence. In *Seager* v. *Copydex (No.1)*[64] the defendants were held to have behaved 'unreasonably' inasmuch as they did not realise, and so refused to acknowledge, the inventive debt their subconscious thought-processes owed to the plaintiff's previous disclosures to them. Nevertheless, they were held liable for breach of confidence, although they had not behaved dishonestly or in conscious bad faith.

In *Talbot* v. *General Television Corp. Pty Ltd*[65] the plaintiff, an independent film producer, developed a concept for a television series. In the course of negotiations with the Channel 9 station in Sydney (operated by Television Corp. Ltd, a N.S.W.

company), he disclosed the concept and later sent the station a copy of a pilot script for his proposed production. He received no further response from the network. Some time later, the plaintiff saw network advertisements for a forthcoming series substantially similar to the one he had proposed. The series was being produced by the Channel 9 station in Melbourne (operated by the defendant). He wrote to the defendant demanding that the series not be broadcast and obtained an interim injunction to this effect. The defendant chose to disobey contending that the original idea for its series had been independently developed by its own employees and that no use had been made of the plaintiff's concept as disclosed to the network's Sydney station. It was revealed in evidence that the defendant's employees had had substantial discussions with the employees of the Sydney station to whom the plaintiff had disclosed his concept and the trial judge held that the final series concept was substantially, if subconsciously, derivative of the plaintiff's original idea. Harris J. explained that:

> the courts are prepared to take judicial notice of the fact that a person may come out with a suggestion which he honestly believes to be a novel suggestion of his own, but which can properly be attributed to his mind having subconsciously used information which he had been given in the past and of which he has no conscious recollection.[66]

The defendant's argument that the plaintiff was not entitled to any relief, on the ground that the defendant was an innocent third party to the Sydney station's breach of confidence, was cursorily dismissed. Harris J. relied on *Stevenson, Jordan & Harrison Ltd* v. *MacDonald & Evans*[67] as authority for his finding that:

> once the defendant had been put on notice that the programme had been made by an unauthorised use of confidential information, then an obligation attached to the defendant not to make any use of it because it would be unconscionable for it to do so.[68]

The judge was also assisted by his finding on the facts that the defendant was a subsidiary of the company which operated the Sydney station so that in effect the network was operated as one enterprise.[69]

This case highlights the analytical niceties inherent in finding a breach of confidence by mere inadvertence. Isn't such a finding very close to finding an 'innocent' breach of duty? If so, the more stringent view postulated above as an alternative to Professor Jones' view would seem to find some support. Or are these cases simply examples of cases where Equity is content to make politic findings on the facts which will provide adequate remedies to an aggrieved party, 'without', as Harris J. said, "attributing fraud or conspiracy or perjury against the defendant's witnesses"?[70]

Questions which arise as to the kind of knowledge the third party had and as to when he acquired that knowledge are essentially questions of fact. The courts will take into account all the relevant circumstances, particularly the kind of confidential information involved, some information being by its very nature and subject-matter more obviously secret, and the manner and form in which the third party acquired it from the misbehaving confidant. If the information is acquired, for example, in the form of tapes made from electronic bugging,[71] stolen documents[72] or surreptitiously made copies,[73] the very form in which the confidential information was conveyed

may be considered enough to put the third party on constructive notice at least of a breach of confidence or some wrongdoing. In such situations, the courts should have little difficulty in holding that the third party would then realise that, if he continues to act as he has been acting, he may take unfair advantage of the plaintiff, especially since in such obvious situations the third party would have to be very bold or naive to assert innocence of any wrongdoing at all.

It is submitted that constructive knowledge should not be imputed to an innocent third party who is in fact totally and reasonably unaware, presumably because the misbehaving confidant has actively misled him that the tapes were made by bugging, the documents stolen or the copies surreptitiously made. He should only be held to have constructive knowledge when the court considers that it would have been unreasonable for him not to suspect a breach of confidence or some wrongdoing. So, if, for example, the third party acquires the information in the form of a diary which has ostensibly been abandoned by its owner (when it was in fact stolen by the misbehaving confidant after the discloser told him of its contents), constructive knowledge should not be imputed to the third party until he becomes aware or should have become aware that he was misled by the misbehaving confidant. In such a situation, the form in which the information was conveyed indicates that the information is confidential but other circumstances negative any inference by the third party of any breach of confidence. Certainly, in the situation where the confidant's breach is by unconscious inadvertence, as in *Seager* v. *Copydex*[74] and *Talbot* v. *General Television Corp. Pty Ltd*[75] and it is a third party who causes injury to the plaintiff actual knowledge of the plaintiff's disclosures to the unconsciously plagiarising confidant would be required to impute constructive knowledge. Certainly there could be no real question as to the third party's actual knowledge of the breach until the plaintiff complains of his injury.

However, recent decisions in the area of conflict of duty and interest have circumscribed the equitable doctrine of notice in ways which may be seen to circumscribe this exposition.[76] It is a general principle of Equity that either actual or constructive notice will suffice to bind the conscience of a wrongdoer.[77] These recent cases have revolved around the issue of whether actual knowledge of wrongdoing, albeit non-specific, is required for an agent of a fiduciary to be held to have constructive notice and therefore to be liable as constructive trustee under the second limb of the rule in *Barnes* v. *Addy:*

> Those who create a trust clothe the trustee with a legal power and control over the trust property, imposing on him a corresponding responsibility. That responsibility may no doubt be extended in equity to others who are not properly trustees, if they are found either making themselves trustees de son tort, or actually participating in any fraudulent conduct of the trustee to the injury of the cestui que trust. But, on the other hand, strangers are not to be made constructive trustees merely because they act as the agents of trustees in transactions within their legal powers...unless those agents receive and become chargeable with some part of the trust property, or *unless they assist knowledge in a dishonest and fraudulent design on the part of the trustees.*[78]

In *Selangor United Rubber Estates* v. *Cradock (No.3)*[79] and *Karak Rubber Co. Ltd* v. *Burden (No.2)*[80], it was held that such an agent was liable as constructive trustee if

a reasonable man in his position ought to have been put on notice to make the relevant enquiries which would have revealed the breach of trust. The Court of Appeal in *Carl Zeiss Stiftung* v. *Herbert Smith (No.2)*[81] rejected this view. As Sachs L.J. said:

> [There must be an] element...of dishonesty or of consciously acting improperly, as opposed to an innocent failure to make...proper enquiry... [A] person wilfully shutting his eyes to the obvious is in no different position than if he had kept them open...[A]n innocent, even if negligent, failure to make enquiries is not enough.[82]

The view of the Court of Appeal seems to collapse the categories of actual and constructive notice into one: for the fiduciary's agent to be liable, he must have actual knowledge of some impropriety, even if its nature is unspecified to him. It seems that it is this more lenient test which has been approved somewhat equivocally by the Australian High Court in *Consul Development Pty Ltd* v. *DPC Estates Pty Ltd.*[83] Barwick C.J. and Stephen J. reaffirmed the pre-*Selangor/Karak* authorities. As Stephen J. said:

> In my view, the state of the authorities as they existed before *Selangor* did not go so far, at least in cases where the defendant had neither received nor dealt in property impressed with any trust, as to apply to them that species of constructive notice which serves to expose a party to liability because of negligence in failing to make enquiry. If a defendant knows of facts which themselves would, to a reasonable man, tell of fraud or breach of trust the case may well be different, as it clearly will be if the defendant has consciously refrained from enquiry for fear lest he learn of fraud. But to go further is, I think, to disregard equity's concern for the state of conscience of the defendant.[84]

The third majority judge, Gibbs J. however, seems to go further than Barwick C.J.'s and Stephen J.'s view that only a wilful 'shutting of the eyes' will be adequate to constitute constructive notice, when he says:

> It may be that it is going too far to say that a stranger will be liable if the circumstances would have put an honest and reasonable man on enquiry when the stranger's failure to enquire has been innocent and he has not wilfully shut his eyes to the obvious. On the other hand, it does not seem to me to be necessary to prove that a stranger who participated in a breach of trust or fiduciary duty with knowledge of all the circumstances did so actually knowing that what he was doing was improper. It would not be just that a person who had full knowledge of all the facts could escape liability because his own moral obtuseness prevented him from recognising an impropriety that would have been apparent to an ordinary man.[85]

So it seems that the Australian position in regard to the precise content of the doctrine of constructive notice is not a definitive one. The views of Gibbs J., and of McTiernan J. in dissent, in the *Consul Developments* case would seem to accord with the exposition given by the writer of the kind of knowledge which would constitute constructive notice in an action for breach of confidence. The view of Barwick C.J. and Stephen J., however, is more lenient to an innocent third party: nothing less than a wilful and conscious shutting of the eyes to impropriety will suffice.

Apart from the two views already discussed, there is a third view which is suggested by Meagher and Gummow in the fourth edition of *Jacob's Law of Trusts in Australia*[86] as a possible solution to the doctrinal dilemmas surrounding the liability of innocent third parties. They, too, take the view that the innocent third party should only be liable to the discloser when he has notice of the confidant's breach of duty. However, unlike Professor Jones who bases his view upon the existence of general restitutionary principles in English law, they claim that this situation is an appropriate one for the imposition of a constructive trust upon the profits made by the third party. They rely upon the second limb of the rule in *Barnes* v. *Addy* in which strangers to a trust are not to be made constructive trustees "unless they assist with the knowledge in a dishonest and fraudulent design on the part of the trustees."[87] Such strangers do not actually have to deal with the trust property themselves for a remedial constructive trust to be imposed. As Gibbs J. said in the *Consul Developments* case, the rule:

> extends to the case where a stranger has knowingly participated in a breach of fiduciary duty committed by a person who is not a trustee even though nothing that might properly be regarded as trust property — even property stamped with a constructive trust — has been received... If the maintenance of a very high standard of conduct on the part of fiduciaries is the purpose of the rule it would seem equally necessary to deter other persons from knowingly assisting those in a fiduciary position to violate their duty.[88]

However, in that same case, Gibbs J. highlighted a fundamental objection to the application of this trust doctrine to the action for breach of confidence, considering that "there is no doctrine of equity imposing a constructive trust as to the profits from misapplied confidential information merely because the stranger has constructive, but not actual, notice of the misapplication"[89] because there is no property in information.

Meagher and Gummow counter this objection in this way:

> One might be permitted to doubt the cogency of the argument: whilst it is true that there is no proprietary right in information or knowledge per se, confidential information has sufficient relevant similarity to trust property in the present connection to require a similar rule to that governing actual property impressed with a trust.[90]

No doubt, there may certainly be situations involving innocent third parties with constructive notice in which the imposition of a remedial constructive trust would provide an adequate compensatory solution. However, it is the present writer's view that it is not wise to use even the analogy of information with property in this way, especially when it has been argued that the defence of bona fide purchase should not be available to such a third party.

However, the real problem is that a remedial constructive trust could only be imposed where the constructive trustee has been guilty of some wrongdoing. With the current state of the constructive notice doctrine in Australia, a constructive trust could only be imposed where the third party was no longer an 'innocent', if he ever was. This means that in the situation[91] where the confidant's breach is by unconscious inadvertence and it is an innocent third party who makes the particular unauthorized use of the confidential information which causes injury to the plaintiff, the discloser would have no compensatory remedy at all.

The difficult task confronting the courts in relation to innocent third parties is to decide which doctrinal solution provides the most flexible and adequate remedies. It is submitted that the prejudice of the court should be equally balanced: on the one hand by a concern to prevent further harm to the discloser and to compensate him for the harm he has suffered as far as it is possible in Equity's compensatory jurisdiction while, on the other hand by a concern to take into account the circumstances of the innocent third party, who may have changed his circumstances substantially to his detriment relying upon his acquisition of and continuing right to use the confidential information; but who also may have other redress against a confidant who has breached his fiduciary duty for fraud or at least, for misrepresentation.

The relief which Equity will grant, in its discretion, to the plaintiff against an innocent third party will depend upon the particular circumstances. Monetary compensation may be adequate in the situation where a trade secret of no 'special' character has been misused,[92] but other situations, particularly but not only, those involving personal confidence, will call for injunctive relief. Indeed, it is to this latter situation that Lord Denning referred in *Fraser* v. *Evans*[93]:

> No person is permitted to divulge to the world information which he has received in confidence... Even if he comes by it innocently, nevertheless once he gets to know that it was originally given in confidence, he can be restrained from breaking that confidence.[94]

In awarding relief, Equity should balance the consequences to be suffered by the third party if relief is awarded against him, with those to be suffered by the discloser if the third party is to be permitted to use or continue to use the confidential information and the discloser merely recompensed for this use in Equity's compensatory jurisdiction. No doubt there are some situations where no consequence of a merely financial nature to be suffered by the third party could outweigh those to be suffered by the discloser, for example situations involving the disclosure of personal biographical information. But there would be other situations where the financial loss to an innocent third party, particularly if that third party had changed his position substantially in reliance on his acquisition of the information, would outweigh any detriment, financial or otherwise, to the discloser. In those situations, the defence of change of circumstances will assist the third party and the discloser would be adequately compensated for the third party's use of that information on the principles outlined in *Seager* v. *Copydex (No.2)*[95] and, on those principles further extrapolated from the case elsewhere by the present writer.[96] The innocent third party could then presumably claim indemnity for this amount of compensation from the misbehaving confidant.

In conclusion, it is submitted that Equity should look as benignly as possible upon the predicament of a third party innocently implicated in another's breach of confidence. The best view is the strict one that an innocent third party to whom the plaintiff's secret has been divulged should be liable from the very moment he acquires knowledge of the plaintiff's secret. However, Equity should take a flexible view of his predicament when considering whether the plaintiff can demand an injunction and/or an account of profits, or merely monetary compensation. Relevant considerations include the third party's honesty, his actual or constructive

knowledge of the breach by the confidant and the general reasonableness of his behaviour in the circumstances. Finally, the availability of the proposed defence of change of circumstances to such a third party would best assist the court in balancing the competing equities of the wronged discloser and the innocent third party, both of whom, it must not be forgotten, have been taken unfair advantage of by the misbehaving confidant.

## FOOTNOTES

1. G. Jones, "Restitution of Benefits Obtained in Breach of Another's Confidence" (1970) 86 *L.Q. Rev.* 463, 473-4.
2. *Cranleigh Precision Engineering* v. *Bryant* [1966] R.P.C. 81, 89-90.
3. Note 1 *supra,* 482: "A plaintiff who does not take reasonable steps to protect the secrecy of information should not be able to claim that another had breached his confidence".
4. *Ibid.*
5. *The Times of London,* 4 July 1981, 1.
6. *Albert (Prince)* v. *Strange* (1849) 1 Mac. & G. 25, 41 E.R. 1171; *Morison* v. *Moat* (1851) 20 L.J. Ch. 513; *Abernethy* v. *Hutchinson* (1824) 1 H. & Tw. 28, 47 E.R. 1313; *International Tools* v. *Kollar* (1968) 67 D.L.R. (2d) 386; *British Steel Corp.* v. *Granada Television* [1981] 1 All E.R. 417.
7. P. D. Finn, *Fiduciary Obligations* (1977) paras 369-372.
8. See text accompanying footnotes 45-59.
9. Note 7 *supra,* para. 370.
10. M. Neave and M. Weinberg, "The Nature and Function of Equities (Part 2)" (1978) 6 *Uni. Tas. L.R.* 115.
11. Note 1 *supra,* 477-481.
12. Note 10 *supra.*
13. J. E. Stuckey, "The Equitable Action for Breach of Confidence: Is Information Ever Property?" (1981) 9(2) *Syd. L.R.* 402; See also note 1 *supra,* 478.
14. *Ibid.*
15. *Stewart* v. *Cook* 45 S.E. 369, 370 Per Candler J. (1903); *Homer* v. *Crown Cork and Seal Co. of Baltimore City* (1928) 141 A. 425, 431 per Parke J.; *Lamont, Corliss and Co.* v. *Bonnie Blend Chocolate Corp.* (1929) 238 N.Y.S. 78; American Restatement of Torts No. 758(b).
16. *Abernethy* v. *Hutchinson* (1824) 3 L.J. Ch. 209; *Albert (Prince)* v. *Strange* (1849) 2 De g. & Sm. 652; *Morison* v. *Moat* (1851) 9 Hare 241, 68 E.R. 492.
17. *Ibid.*
18. *Ibid.*
19. *Ibid.*
20. *Ibid.*
21. 9 Hare 241, 263-4; 68 E.R. 492, 501-502.
22. See also *Nicrotherm Electrical Co. Ltd* v. *Percy* [1957] 74 R.P.C. 207, 215 where Romer J. approves what Turner V.C. said about the defence in *Morison* v. *Moat.*
23. [1965] R.P.C. 239.
24. *Id.,* 253.
25. (1968) 67 D.L.R. (2d) 386.
26. *Id.,* 392.
27. (1951) 68 R.P.C. 190; (1952) 69 R.P.C. 10.
28. (1951) 68 R.P.C. 190, 195.
29. Note 21 *supra.*
30. Note 28 *supra.*
31. Note 1 *supra,* 481. See also note 10 *supra,* 125.
32. (1952) 69 R.P.C. 10, 16.
33. Note 1 *supra,* 477.
34. *Ibid.*
35. *American Restatement of Torts,* Section 758, Comment, 22.
36. Note 1 *supra,* 477.
37. *Ibid.*
38. Note 7 *supra,* para. 372.

39. Note 10 *supra,* 124.
40. *Ibid.*
41. See text accompanying footnote 14.
42. W. R. Cornish, "Protection of Confidential Information" (1975) 6 *Int. Rev. of Ind. Prop. and Copyright Law* 43, 55.
43. Note 10 *supra,* 124.
44. *Mustad* v. *Dosen* [1963] R.P.C. 41.
45. (1948) 65 R.P.C. 203, 213.
46. [1967] 1 W.L.R. 923, 931.
47. For discussion of this view see Stuckey, note 13 *supra,* 407-409.
48. Note 7 *supra,* para. 364.
49. *Id.,* paras 1-57 and 321-3.
50. [1981] 2 W.L.R. 848, 869.
51. Note 1 *supra,* 477.
52. Note 45 *supra.*
53. Note in this connection the cases in which it has been held that the duty of confidence may be breached by mere inadvertence in situations where the defendant was not considered to have acted in conscious bad faith: *Seager* v. *Copydex (No. 1)* [1967] 1 W.L.R. 923; *Talbot* v. *General Television Corp. Pty Ltd* [1980] V.R. 224.
54. It can be argued, however, that perhaps Lord Greene M.R. only intended his definition of the duty to extend to third parties with notice of the confidant's breach and not to innocent third parties, if his subsequent reference to *Morison* v. *Moat* is considered as a restrictive one: (1948) 65 R.P.C. 203, 213.
55. Note 1 *supra,* 477: "The defendant's honesty may, however, be an important factor in determining whether the plaintiff can obtain an injunction and/or an account of profits".
56. Note 46 *supra.*
57. Note 7 *supra,* para. 373, n. 37.
58. Note 54 *supra.*
59. Note 57 *supra.*
60. Note 1 *supra,* 476.
61. *Ibid.*
62. Note 53 *supra.*
63. *Ibid.*
64. *Ibid.*
65. *Ibid.*
66. *Id.,* 239.
67. (1951) 68 R.P.C. 190.
68. Note 53 *supra,* 239-240.
69. The highly technical nature of this argument was obviously well-appreciated by counsel since no attempt was made to argue any defence based upon bona fide purchase by the defendant.
70. Note 68 *supra.*
71. Note 16 *supra.*
72 *British Steel Corp.* v. *Granada Television* note 6 *supra.* See also *The Commonwealth of Australia* v. *John Fairfax & Sons* (1980) 32 A.L.R. 485.
73. *Albert (Prince)* v. *Strange* note 6 *supra.*
74. Note 53 *supra.*
75. *Ibid.*
76. See J. D. Heydon, "Recent Developments in Constructive Trusts" (1977) 51 *A.L.J.* 635.
77. R. E. Megarry and P. V. Baker (eds), *Snell's Principles of Equity* (27th ed. 1973) 50 ff.
78. (1874) 9 Ch. App. 244, 251-2 per Ld Selborne L.C.
79. [1968] 1 W.L.R. 1555.
80. [1972] 1 W.L.R. 602.
81. [1969] 2 Ch. 276.
82. *Id.,* 298.
83. (1975) 132 C.L.R. 373.
84. *Id.,* 412.
85. *Id.,* 398. It is important to note, however, that Gibbs J. did not consider it necessary to decide this issue conclusively for his decision in the *Consul Developments* Case.
86. (1977) para. 1321.
87. Note 78 *supra.*
88. Note 83 *supra,* 396-7.

89. Note 86 *supra.*
90. *Ibid.*
91. See text accompanying footnotes 70-75.
92. Note 13 *supra,* 415 ff.
93. [1969] 1 Q.B. 349.
94. *Id.,* 361.
95. [1969] 1 W.L.R. 809.
96. Note 92 *supra. Cf.* judgments of Full Court in *Talbot* [1980] V.R. 224 concerning the assessment of compensation for breach of confidence.