[HIGH COURT OF AUSTRALIA.]

FURS LIMITED . . . . . APPELLANT;
PLAINTIFF,

AND

TOMKIES AND OTHERS . . . . . RESPONDENTS.
DEFENDANTS,

ON APPEAL FROM THE SUPREME COURT OF NEW SOUTH WALES.

H. C. OF A. 1935-1936.

SYDNEY, 1935, *Oct.* 18, 21, 22, 23.

MELBOURNE, 1936, *Feb.* 13.

Latham C.J., Rich, Starke, Dixon, Evatt and McTiernan JJ.

Company—Director—Fiduciary capacity—Conflict between interest and duty—Profit derived from execution of fiduciary duties—Non-disclosure—Liability to account.

T., while managing director of the appellant company, was authorized by the directors to negotiate for the sale of the tanning, dressing and dyeing part of its business. He eventually arranged with L., who was the promoter of a company to be formed, to sell it to that company for £8,500. Pursuant to this arrangement the plaintiff sold to the defendant F. D. Ltd. T. was an expert in the processes of tanning, dressing and dyeing and was familiar with the secret formulae used by the appellant for these purposes. In the course of the negotiations for sale L. told him that the new company would want his services, and he so informed the appellant's chairman of directors. The chairman, after consultation with some of the other directors, advised him to make the best arrangement for himself that he could with the purchaser. Before the terms of sale were agreed upon T. arranged a contract between himself and the company to be formed in which it was agreed that he should serve that company and in that service disclose all his knowledge and information about the processes of the tanning, dressing and dyeing and should receive shares in the company and £4,000, in addition to an annual salary. This transaction, which if carried out would make its formulae valueless to it, was not disclosed to the appellant. After its incorporation F. D. Ltd. adopted the contract with T., issued the shares to him and gave him promissory notes for the £4,000.

Held that T. while acting for the appellant in a fiduciary capacity had derived undisclosed benefits for himself for which he was accountable to the

H. C. OF A. 1935-1936.

FURS LTD. v. TOMKIES.

appellant. If it were a fact that the appellant did not suffer any loss corresponding to the benefits derived by T., that fact did not affect the duty of T. to account for the benefits derived.

Decision of the Supreme Court of New South Wales (*Nicholas* J.) reversed.

APPEAL from the Supreme Court of New South Wales.

Furs Ltd., brought a suit in the Supreme Court of New South Wales against Gordon Watson Tomkies, Fur Dressers and Dyers Ltd., Lionel Lumb and Arthur Pratt, claiming (by pars. 1-5 of the prayer in the statement of claim) a declaration that 500 preference shares and 500 ordinary shares held by Tomkies in Fur Dressers and Dyers Ltd. belonged to it and an order that the shares be transferred to it and an order that Tomkies pay and transfer to it all moneys and securities received by him from the other defendants or any of them in or to secure payment of a sum of £4,000 payable to him under contracts between him and Pratt and Lumb dated 6th September 1929 and between him and Fur Dressers and Dyers Ltd., Pratt and Lumb dated 31st October 1931 and an order restraining the other defendants from paying or transferring such moneys or securities to any person other than it.

The defendants, other than Tomkies, entered appearances whereby they submitted to any order or decree that the Court might see fit to make. In its statement of claim the plaintiff alleged that Tomkies had received the shares and money in question from the other defendants as consideration for the sale of certain secret formulae which belonged to the plaintiff, but which were represented by Tomkies as belonging to him. Alternatively it was alleged that Tomkies received such property as a fraudulent and secret profit made and obtained by him while acting as a director of the plaintiff. At the hearing the statement of claim was amended to claim the property on the ground that it was an undisclosed profit received by Tomkies while acting for the plaintiff in a fiduciary capacity.

Nicholas J. found that Tomkies did not sell the formulae as his own and that, although he received the property while acting in a fiduciary capacity in such circumstances that his own interests might conflict with his duty to the plaintiff, yet he was put in that position by the plaintiff and was entitled to secure his own advantage

so long as he treated the plaintiff fairly, and that as no breach of that duty had been proved the action failed.

From this decision the plaintiff now appealed to the High Court.

Further facts appear in the judgments hereunder.

Spender K.C. (with him *Gain* and *Mackay*), for the appellant. The defendant received the shares and £4,000 as consideration for the sale of assets belonging to the plaintiff. Those assets consisted either in the actual formulae, which the appellant's evidence shows that Tomkies falsely represented to be his own, or in the knowledge which he acquired in the plaintiff's business, which belonged to it and which Tomkies contracted for his own benefit to disclose (*In re Keene* (1); *Amber Size and Chemical Co. Ltd.* v. *Menzel* (2); *Herbert Morris Ltd.* v. *Saxelby* (3)). Even if the directors of the plaintiff knew of this the plaintiff is still entitled to succeed (*Cook* v. *Deeks* (4)). Tomkies was acting in a position where his interest conflicted with his duty and any advantage he received belongs in equity to the plaintiff, to whom he owed the duty (*Transvaal Lands Co.* v. *New Belgium (Transvaal) Land and Development Co.* (5); *Costa Rica Railway Co. Ltd.* v. *Forwood* (6); *Aberdeen Railway Co.* v. *Blaikie Brothers* (7); *Prebble* v. *Reeves* (8); *Bendigo Central Freezing and Fertilizer Co. Ltd.* v. *Cunningham* (9)). Though it is not necessary to go so far, the evidence establishes that while acting in a position where his interest conflicted with his duty he preferred his interest to his duty (*Wright* v. *Morgan* (10)). Tomkies' conduct was not authorized by the plaintiff company. He was not authorized to do what he did by the articles of association or by the board of directors (*D'Arcy* v. *Tamar, Kit Hill and Callington Railway Co.* (11); *Demerara Bauxite Co.* v. *Hubbard* (12); *Moody* v. *Cox and Hatt* (13)).

Dudley Williams K.C. (with him *McMinn*), for the respondent Tomkies. Tomkies was under a duty to the plaintiff to serve it

(1) (1922) 2 Ch. 475.
(2) (1913) 2 Ch. 239.
(3) (1915) 2 Ch. 57.
(4) (1916) 1 A.C. 554.
(5) (1914) 2 Ch. 488.
(6) (1901) 1 Ch. 746.
(7) (1854) 1 Macq. 461.
(8) (1910) V.L.R. 88.
(9) (1919) V.L.R. 387.
(10) (1926) A.C. 788.
(11) (1867) L.R. 2 Ex. 158.
(12) (1923) A.C. 673.
(13) (1917) 2 Ch. 71.

H. C. OF A. 1935-1936. FURS LTD. v. TOMKIES.

faithfully. This is the only stipulation to be implied (*Wessex Dairies Ltd.* v. *Smith* (1)). The trial Judge found that he fulfilled this duty. He also found that he did not sell anything not his own. These conclusions should be accepted (*Powell* v. *Streatham Manor Nursing Home* (2)). Tomkies was entitled to sell his own skill and ability (*Ormonoid Roofing and Asphalts Ltd.* v. *Bitumenoids Ltd.* (3)). Tomkies was authorized in advance by the board of directors to do what he did. The case is similar to *Hordern* v. *Hordern* (4). A board can meet effectively in informal circumstances (*Barron* v. *Potter* (5)). The plaintiff has suffered no damage by reason of the arrangement Tomkies made for himself. The purchaser would not have purchased had Tomkies refused to enter its employ. Tomkies obtained for the plaintiff the maximum price obtainable.

Spender K.C., in reply. In so far as the *Ormonoid Roofing Case* (3) decides that what an employee has learnt in the course of his employer's business and carries in his own head is his property and not that of his employer, it is inconsistent with the authorities cited. Once it is established that a person employed in a fiduciary capacity has acted in such a way that his interest and duty conflict it is not necessary to consider what did in fact take place (*Wright* v. *Morgan* (6)).

Cur. adv. vult.

1936 Feb. 13. The following written judgments were delivered :—

LATHAM C.J. The plaintiff company was carrying on in Sydney the business of manufacturing furs for coats and ladies' stoles, and of tanning, dyeing, and dressing skins. In 1929 the chairman of directors was Mr. F. W. Cropley and the defendant Mr. G. W. Tomkies was the managing director of the company ; he was also the manager of the tanning, dyeing and dressing branch of the business. He had special knowledge of the tanning, dyeing and dressing branch of the business which had been developed under

(1) (1935) 2 K.B. 80.
(2) (1935) A.C. 243.
(3) (1931) 31 S.R. (N.S.W.) 347 ; 48 W.N. (N.S.W.) 66.
(4) (1910) 10 S.R. (N.S.W.) 677.
(5) (1914) 1 Ch. 895.
(6) (1926) A.C. 788.

his management. He had been sent abroad at the cost of the company and was in possession of formulae and of knowledge of processes of manufacture which were regarded as of very considerable value.

Early in 1929 this branch of the business was seen to be unsuccessful and Tomkies suggested to his co-directors that, for trade reasons, it should be conducted by a separate company or that it should be sold. This matter was discussed at meetings of the board of directors. About June Mr. Lionel Lumb, who represented a New Zealand company, visited the factory and later a letter was received from New Zealand inquiring whether the plaintiff was prepared to sell this branch of its business. After discussion between the directors, on 25th June 1929, the defendant Tomkies (hereinafter referred to as the defendant) wrote a letter as managing director referring to the proposed sale and stating that the complete plant including certain machinery and chemicals "would be worth approximately £8,500, but the matter which would need most consideration would be the value of working formulas, and compensation for the amount of work we have put into this end of the business in bringing it to perfection."

On 18th July the defendant wrote another letter addressed to the defendant, Fur Dressers and Dyers Ltd., emphasizing the value and importance of the working formulae, declining to give particulars of them at that stage of the negotiations, and stating that in addition to the £8,500 already mentioned the plaintiff company "would want £5,500 for the formulas and the business as a going concern."

Lumb came to Sydney in August 1929 and the proposal for sale was discussed in the first instance between the defendant and Lumb.

On 20th August 1929 Lumb and the defendant had a conversation in the course of which Lumb said that before he could go any further with his plans he had to be assured that the defendant's services would be available to the new dressing, dyeing, &c., company which it was proposed to establish. The defendant repeated this statement to Cropley, the chairman of directors of the plaintiff company, and Cropley said that if the plaintiff company sold the branch of its business which was under discussion it could not afford

H. C. OF A. 1935-1936.

FURS LTD. v. TOMKIES.

Latham C.J.

to keep the defendant on its staff, and he added: "I would advise you to make the best deal you can in the new company."

Cropley died before the action came to trial but the learned Judge accepted the evidence of the defendant that this statement was made. Then Lumb and the defendant discussed the details of the agreement to be made between the new company and the defendant. Lumb said that the purchaser would want the defendant to go to New Zealand and possibly to Melbourne and "to organize the factory and teach anyone we might nominate the application of the formulae we might buy from Furs Ltd." Defendant said: "The practical knowledge that I have obtained in the application of the formulae and the technical side of the business has been gained by me during ten years practical experience, and if I am to go to New Zealand or to Melbourne or anywhere else and teach your employees or anyone you might nominate all I have learned about the dressing and dyeing business, in a very short time my position would not be secure." The defendant and Lumb arrived at an arrangement under which the defendant would become an employee of the purchaser (or of a company to be formed by it) for a period of three years, the defendant binding himself by a restrictive covenant for a period of five years after the determination of the agreement, and the purchaser agreeing to pay a salary of £20 per week and a further sum of £5,000, to be satisfied partly by shares in the new company and partly by guaranteed promissory notes.

Several documents relating to this arrangement were drawn up from time to time, and in some of them it was stated that the defendant was receiving the consideration mentioned as the price of the formulae, or as a remuneration for procuring the plaintiff to enter into the contract for the sale of the business. The learned Judge did not, however, accept this view of the transactions, but, on the other hand, accepted the defendant's explanation that the documents were prepared in this form in order to justify, from a legal point of view, the issue to the defendant of paid up shares in the company which was to be formed and the making and delivery to him of promissory notes for the balance of £4,000.

After making this arrangement with Lumb the defendant went to the chairman of directors and discussed the proposals for the sale of

the business by the company. He then again saw Lumb, and a day or two later Lumb told him that £8,500 was as much as he would give for the plant and the formulae. The defendant reported this to Cropley who said he thought they should not miss the chance of business and that the offer should be accepted.

On 29th August the board of directors met, and, after the matter had been discussed, agreed to make an offer to sell the business plant and formulae for £8,500. This offer was accepted by Lumb. On 19th September a meeting of the shareholders &c. was held and the shareholders were informed that the sale had been effected for a sum of £8,500.

Neither the directors nor the shareholders were told that the defendant was receiving a sum of £5,000, and the defendant took pains to prevent this becoming known. The chairman of directors, Cropley, was aware that the defendant was receiving some consideration in connection with the transaction, and that this fact had caused anxiety and concern to Mr. York, the solicitor who was employed by Lumb, as well as by the plaintiff, in connection with the preparation of the necessary legal documents. The defendant, however, refused to give Cropley the particulars of his agreement, and Cropley abstained from making further inquiries.

As I have already mentioned, some of the documents purport to record a sale of the formulae by the defendant as if they were his own property. The learned Judge, however, was satisfied that this was not the real transaction, and he accepted the explanation given by the defendant. The plaintiff company claims that the defendant, being in a fiduciary position, was guilty of a breach of duty, and that, even if he did not sell the property of the company as if it were his own property, he was nevertheless responsible for any damage caused to the company by his wrongful act or that he became liable to pay to the plaintiff the amount of profit he himself made by reason of the breach of duty.

The defendant was in a position where his interest conflicted with his duty. As director of the company entrusted with negotiations for the sale of assets of the company, it was his duty to do his best for the company by obtaining the best price it was possible to obtain upon the sale of the business, including the plant and the formulae.

H. C. OF A. 1935-1936.

FURS LTD. v. TOMKIES.

Latham C.J.

From the point of view of his own personal interests, he would naturally wish to make the best possible agreement for himself in the new employment which had become available to him. It was very important for him to arrange for his own future employment, because the sale of the branch of the plaintiff's business with which he was particularly associated would deprive him of the position which he then held.

There was thus a plain conflict of duty and interest. In such circumstances it was his duty to put the company first. The statement of the chairman of directors (or even the statement of the whole board of directors) that he could do his best for himself was an intimation that, so far as the company was concerned, he was at liberty to accept the position offered to him on the best terms he could get. But in the first place, in my opinion, it is not a fair interpretation of that intimation to say that he was thereby authorized to subordinate the interests of the company to his own. Further, if the directors did purport to give him such an authority, their action would be ineffectual. It would involve a breach of their duty to the company, and the defendant himself would be a party to that breach of duty. The directors were not at liberty to determine, in favour of any of their own body, that the rights of the company should be disregarded (cf. *Cook* v. *Deeks* (1)).

It has been said that the position was a difficult one for the defendant. In a sense this was the case. But there is really nothing unusual in the requirement that a person occupying a position of trust and confidence should subordinate his own interests to the interests of another person to whom he stands in a fiduciary relation. The defendant might have proposed the postponement of any discussion of the terms upon which he would accept employment until after the agreement of sale had been made for the plaintiff company, or he might have offered to retire altogether from the negotiations as soon as the difficulty became apparent. It is true that the purchaser might have refused to continue negotiations until he had made sure that the defendant would carry on with the new owner of the business upon satisfactory terms. In that event the proper course for the defendant to adopt, if the negotiations

(1) (1916) A.C. 554, at p. 564.

went on, was to make a full disclosure to the shareholders of the arrangements which he had made on his own behalf with the company to which the plaintiff was selling its business. In fact, however, he made an agreement with respect to his own interests first, and the negotiations then proceeded between Lumb and the plaintiff (represented in part by the defendant and in part by Cropley) upon the basis, known to Lumb and the defendant, but not known to any of the other directors or to the shareholders of the company, that the purchaser had already agreed to pay Tomkies £5,000 in addition to a salary.

The effect of this procedure was that the formulae for which the company had asked £5,000 became practically valueless. The defendant in cross-examination admitted that this was the case. He said not only that the value of the formulae would be decidedly depreciated, but also that there would not be any value left at all if, before the company arranged the terms of its sale, he had agreed to disclose the formulae ; and he admitted, consistently with the evidence which he gave, that he had so agreed.

It was strongly urged that the plaintiff company had lost nothing by reason of the action of the defendant because £8,500 was the maximum amount which the purchaser was prepared to give. The references which I have made to the evidence show, however, that this sum of £8,500 is a maximum which was mentioned only after the purchasing company had agreed to pay Tomkies £5,000 in addition to a salary.

At the time when the matters to which I have referred took place the defendant was still managing director of the plaintiff company and he did not resign his position as director until 30th October 1929.

In what I have said I have accepted the findings of fact made by the learned Judge but I have indicated the legal significance which I think that certain of them should properly bear. Upon this basis of fact I think that the plaintiff should succeed in the action. In my opinion, the defendant was guilty of a breach of fiduciary obligation by which he has profited at the expense of the company. It is impossible to say that the loss to the company is measured by the profit to the defendant. Such an inquiry is a mere matter of

H. C. OF A. 1935-1936.

FURS LTD. v. TOMKIES.

Latham C.J.

conjecture. But the obligation to account for such a profit does not depend upon the possibility of showing that the person entitled to complain of the breach of duty has suffered pecuniary damage to an equivalent extent. In my opinion, the defendant is bound to account for the paid up shares and the promissory notes or the proceeds thereof because they were an undisclosed profit received by him in the course of a transaction in which he occupied a fiduciary relationship to the company and by reason of his breach of the obligation upon which the rules of equity insist in such a case.

RICH, DIXON AND EVATT JJ. In our opinion the decision of this appeal is governed by the inflexible rule that, except under the authority of a provision in the articles of association, no director shall obtain for himself a profit by means of a transaction in which he is concerned on behalf of the company unless all the material facts are disclosed to the shareholders and by resolution a general meeting approves of his doing so, or all the shareholders acquiesce. An undisclosed profit which a director so derives from the execution of his fiduciary duties belongs in equity to the company. It is no answer to the application of the rule that the profit is of a kind which the company could not itself have obtained, or that no loss is caused to the company by the gain of the director. It is a principle resting upon the impossibility of allowing the conflict of duty and interest which is involved in the pursuit of private advantage in the course of dealing in a fiduciary capacity with the affairs of the company. If, when it is his duty to safeguard and further the interests of the company, he uses the occasion as a means of profit to himself, he raises an opposition between the duty he has undertaken and his own self interest, beyond which it is neither wise nor practicable for the law to look for a criterion of liability. The consequences of such a conflict are not discoverable. Both justice and policy are against their investigation. With reference to a transaction arising out of another relation of confidence, Lord *Eldon* said : " The general interests of justice " require " it to be destroyed in every instance ; as no Court is equal to the examination and ascertainment of the truth in much the greater number of cases "

(*Ex parte James* (1)). His language has been applied to, and illustrated by, the case of a fiduciary agent making undisclosed profits (*Panama and South Pacific Telegraph Co.* v. *India Rubber Gutta Percha and Telegraph Works Co.* (2)).

The present case supplies another example of the difficulties which beset any examination of the effect upon the transaction entered into by the company produced by the incidental enrichment of a director concerned in carrying it out.

The director is the respondent. The transaction was the sale of a branch of the company's manufacturing business. The branch, which consisted in the dyeing and dressing of furs, had been established at the instance of the respondent and he conducted it as manager. He had been sent abroad by the board of directors of which he was a member to acquire at the company's expense a knowledge of the art, and, in the course of his inquiries in other countries, he had secured on behalf of the company chemical formulas or recipes which were considered valuable and kept secret. The dyeing and dressing branch appears to have been successful in the quality of its work but to have failed, for trade reasons, in obtaining the custom of outside furriers. For this reason and because the burden of the respondent's salary, £1,000 a year, could not be neglected among the financial difficulties which, in the year 1929 the company began to feel the board of directors decided to dispose of the branch.

While upon a visit to Sydney the director of a New Zealand company carrying on a similar enterprise inspected the factory. He was impressed with its products and with the management of the respondent. Before his return to New Zealand his company received from the appellant company a letter over the signature of the respondent as managing director offering its fur dressing and dyeing business for sale. The letter named £8,500 as the price of the plant, but added that what would need most consideration would be the value of the working formulas and compensation for the work which had been put into that branch of the business. A later letter asked £5,500 for the formulas and " business as a going

(1) (1803) 8 Ves. 337, at p. 345; 32 E.R. 385, at p. 388.

(2) (1875) L.R. 10 Ch. 515, at pp. 523, 527.

H. C. OF A. 1935-1936.

FURS LTD. v. TOMKIES.

Rich J. Dixon J. Evatt J.

concern " in addition to the £8,500 for the plant. The New Zealand director then came back to Sydney to continue the negotiations.

On the side of the appellant company, the chief part in them was taken by the respondent. At an early stage, apparently, it became clear that the proposing purchasers required that the respondent should come over with the business. When he reported this to his fellow directors, they told him that their company could not employ him after the sale of the fur dressing and dyeing branch and advised him to look after himself and to make the best terms he could for his services with the purchasing company. That advice he acted upon without delay. On the afternoon of the same day, he met representatives of the purchasing company and, after some discussion of what he would be called upon to do, consented to go over with the business at the same salary as he was receiving and to give a covenant not to compete for five years after the end of his service. But this consent was subject to the proviso that the purchasing company would pay him in cash and shares a lump sum of £5,000 which he demanded. The demand was conceded and they agreed to give him £1,000 in shares and to secure £4,000 by promissory notes payable over four years. This settled, the negotiations on behalf of the company were resumed. In the course of the next few days, proposals were made for a consideration in shares, but the chairman and directors of the appellant company would entertain nothing but an offer of cash. When this was put to the purchasers, according to the respondent's version, they refused to offer more than £8,500 and this refusal he reported to his board, who had looked for a price of £13,000. After some consideration they accepted the offer. In doing so they appear chiefly to have been influenced by a desire to relieve themselves of the current expenditure which arose out of the fur dressing and dyeing branch and to obtain ready money. They knew nothing of the arrangement that the respondent should receive £5,000. He told them, in effect, that the purchasers had found that more money was called for by the business than they had expected, but he did not divulge to his fellow directors that he was the cause of a burden of £5,000. As a result, no doubt, of this suppression he now finds himself faced in these proceedings with a demand that he should account as for a secret profit.

An agreement having been reached, a draft option appears to have been roughly prepared. It covered, among other things, formulas and "also the services of certain personnel." On the same day, the purchasers gave to the respondent a letter saying that as consideration for his procuring for them from the appellant company the equipment of their dressing and dyeing business, all their formulas, a lease of their premises and having himself agreed to associate himself with them as a consulting technical expert, they undertook to deliver to him promissory notes for £4,000 and fully paid shares for £1,000. He accepted the document; but the description of the consideration which it contains did not upon the hearing prove fatal to his case, as it well might have done. For he explained it away in his evidence by saying it was an incorrect record of the transaction and that when he received it he remarked that the first three things to which it referred had nothing to do with him.

The fact that he was to receive a payment was not kept a close secret. He, his chairman of directors, and the representative of the New Zealand purchasers went together to the solicitor who acted for the appellant company and instructed him on behalf of both parties to prepare the necessary instruments to carry out the sale of the fur dressing and dyeing section of the business. Afterwards, on the same day, the solicitor received instructions from the purchasers concerning various matters, including, probably, the preparation of the service agreement between them and the respondent. At any rate, the solicitor learned of the payment that had been arranged. He thought it necessary in the circumstances to refuse to act for both parties and, upon his informing the chairman of the appellant company of this decision, the latter guessed that the cause consisted in knowledge obtained of some illicit payment. He appears to have had no further information than the solicitor's assent to his surmise, but, after consulting two of his co-directors, the chairman resolved to pursue the matter no further for fear the sale should go off. He found, however, that the simple expedient of refusing to recognize the respondent sufficed to make him aware of his suspicions and his feelings. A fortnight or so afterwards he asked the respondent if he might see his service agreement, but the respondent evaded the question and wrote asking

H. C. OF A. 1935-1936.

FURS LTD. v. TOMKIES.

Rich J. Dixon J. Evatt J.

the solicitors to give no information until he returned to Sydney from a holiday he contemplated. Among the provisions of the agreement of sale was one by which the appellant company agreed that the formulas and secret processes acquired for it by the respondent and all other formulas and processes used by it, all being described as within the knowledge of the respondent, should become the property of a company to be formed by the purchasers, that they should be handed over by the respondent in a sealed envelope and that it should be lawful for him after the completion of the sale to disclose any further or additional information that might have come to his knowledge in relation to such formulas and processes while in the service of the appellant company. On the day after the execution of this agreement, the respondent and the representative of the purchasers on behalf of the company to be formed executed a service agreement by which he agreed to serve the company for three years, to give them the benefit of his knowledge and experience in the treatment, dressing and dyeing of furs and in the use of formulas and chemicals and to disclose all the information in his knowledge or power. He agreed that, during the term of his employment and for three years thereafter, he would not divulge to others any of the formulas, secret processes, or methods of treatment employed in the business, and that, for five years after the termination of his employment by the intended company, he would not in the southern hemisphere take part or be concerned in any similar business. " For the consideration aforesaid," it was agreed that he should receive promissory notes for £4,000 and shares for £1,000.

A fortnight afterwards, the respondent vacated his position as manager for the appellant company. Possession of the undertaking was given at the end of about another month. Not long afterwards the new company was registered and the respondent ceased to be a director of the appellant company.

Another new company was also registered by the purchasers. It was called " Fur Developments Ltd." A document was produced and put in evidence consisting of an undated service agreement between the respondent, this new company and some directors as guarantors. It contained interlineations substituting a company to be formed for the new company. The signatures had been cut off

because, according to the evidence, the agreement had ceased to operate. Drafts of agreements between this company and the respondent were also produced. In all these documents the respondent was represented as selling to it as his own property the secret processes or formulas in consideration of promissory notes and shares for £5,000. These documents were explained as intentionally departing from the truth of the transactions in order to provide the second new company with a consideration sufficient to justify the allotment of fully paid up shares and also, presumably, the payment of the promissory notes. They were proved to belong to a date some little time later and this explanation was accepted as true by *Nicholas* J., who heard the suit. The promissory notes were issued by the first of the new companies and in his receipt for them the respondent described them as the purchase price of the formulas. Still later that company acknowledged the receipt of the written formulas from the respondent. The acknowledgement described them as offered by the respondent and accepted for £1,000 cash and £4,000 in promissory notes and it admitted that the company now had no further claim upon him. These documents are explained on the same ground.

It is evident from this brief account of the course of the transaction that, as between the respondent and the purchasers, there has been much fluctuation in the view taken of the nature of the payment of £5,000. The documents represent it successively as a remuneration for procuring the sale, as a lump sum consideration for entering into the service agreement, and as the price of the formulas and the secret processes.

The respondent gives the sum the complexion of present remuneration for future services and benefits, including the use of the skill and knowledge personal to himself and the instruction of others therein and the giving of the covenant in restraint of subsequent competition.

The fact was that he occupied an exceptional situation. He was manager of the section of the business under offer and armed with all the knowledge used in conducting it, whether knowledge forming part of the stock he was entitled to carry away from the appellant company's employment or secret information to which that company

H. C. OF A. 1935-1936.

FURS LTD. v. TOMKIES.

Rich J. Dixon J. Evatt J.

alone was entitled. He was the director to whom the negotiation of the sale had been largely entrusted. No doubt, too, his influence with his board was not negligible. When he demanded £5,000, it is not surprising that the purchasers thought good reason existed for paying it to him. They did not stop to analyse the ingredients in the situation which enabled him to ask for a lump sum. They expressed the payment one way in their preliminary letter, probably without any particular design. The solicitor expressed it in another way in the service agreement he drew up, probably seeking the most plausible and respectable basis on which the payment could be justified. When, later on, they required a consideration to support an issue of shares, the purchasers described it in a third way. There was some ground for each of the complexions given to the payment. It wore more than one aspect. But the fact of paramount legal significance is that the payment was obtained by the respondent in course of a transaction which he was carrying out on behalf of the company in execution of his office of managing director. It was only because it fell to his lot to negotiate the sale on behalf of his company that he was able to demand and obtain the sum. His fiduciary character was alike the occasion and the means of securing the profit for himself.

To our minds it is quite plain that, by doing so, he greatly diminished the price obtainable by the company. He himself admitted on his cross-examination that his entering into the service agreement decidedly depreciated the formulas as an asset for sale and that no value would be left in them. It is not improbable that the price which the company might have got was diminished to the full extent of £5,000. But this is just one of the inquiries that is excluded. So too, on the question of liability to account, is the inquiry into the advantages which the purchasers expected, or had a right to expect, in return. The respondent had a plain duty with which he brought his private interest into conflict and that is enough.

Upon the question what was his profit for which he is liable to account, the respondent is quite at liberty to urge that, in order to gain the £5,000, he parted or agreed to part with something that was his own. But, upon this question, we think the burden of proof lies upon him and the difficulty is to see what exactly it was and what

was its value. It was not the formulas. They were not his. It was not future services because, not only were they remunerated by a salary, but the amount of £5,000 remained payable, although the service agreement should end next day under its resolutive conditions. Nor was it the covenant restraining competition. Such a covenant is allowable for the purpose only of protecting interests which are exposed to a risk of injury through taking a servant into an employment and thus giving him an opportunity of obtaining skill and experience which may be turned to the employer's disadvantage. It cannot simply be bought.

The respondent stipulated for a payment and it appears to us to be altogether a profit.

The case presents no analogy to the sale by a fiduciary agent to his principal of tangible property which, although the principal does not know it, belongs to the agent but was not acquired by him in the course of the agency. In such a case, in the present state of the authorities, rescission seems to be the only remedy (*In re Cape Breton Co.* (1); *Burland* v. *Earle* (2); *Jacobus Marler Estates Ltd.* v. *Marler* (3)). There is no transaction by the directors with the company, nothing for it to rescind. No doubt his co-directors' action in confiding the negotiations to the respondent and advising him to look after himself exposed him to the temptation of preferring his own advantage to the interests of the company. But the board could not relieve him of the equitable obligations which arose out of this conflict of duty and of private interest. His one resource, if he was resolved to adopt the unwise course of acting in the transaction on behalf of his company and yet seeking a profit for himself, was complete disclosure to and confirmation by the shareholders. But complete disclosure he was not prepared to make.

We are unable to agree with the view that the respondent's principal placed him in a position in which his duty and interest conflicted and thus waived the right to the performance of an undivided duty. The board of directors could not do this in the case of a fellow director and, even if it could, no one contemplated anything but an ordinary agreement of employment at a salary. Nor did the board assume

(1) (1885) 29 Ch. D. 795. (2) (1902) A.C. 83.
(3) (1913) 85 L.J. P.C. 167n.

H. C. OF A. 1935-1936.

FURS LTD. v. TOMKIES.

Rich J. Dixon J. Evatt J.

to release him from his duties as manager. It is immaterial, if it be the case, that, unless he had agreed to go over with the business, no sale would have taken place.

In our opinion the appeal should be allowed.

The relief craved by pars. 1, 2, 3, 4 and 5 of the prayer in the statement of claim appears appropriate.

The respondent should pay the costs of the appeal and the suit.

STARKE J. Persons in fiduciary positions are not permitted to acquire any personal benefit in the execution of their trusts or agencies. Thus agents may not acquire any personal benefits in the course of or by means of their agency without the knowledge and consent of their principals. Directors and officers of companies cannot retain any personal benefits acquired in the conduct of the companies' business unless the particulars of such benefits are disclosed to and approved by the shareholders. They must account for and pay over every profit so acquired (*Parker* v. *McKenna* (1)). The rule of law has long been settled, and the argument of the case proceeded accordingly. The contest is as to the facts and the inferences to be drawn from the facts established by the evidence.

Furs Ltd., the appellant here, carried on the business of manufacturing furs, fur coats, and stoles, and dyeing and dressing skins, for itself and other manufacturers. It was possessed of secret or business processes for tanning, dyeing and dressing skins. Tomkies, the respondent here, was originally employed by the appellant as its business manager. He was sent by the appellant on a business visit to Europe and America, and acquired in the course of his travels considerable information as to tanning, dyeing and dressing skins, and particulars of various processes for use in those operations. Ultimately the respondent became the managing director of the appellant company at a remuneration of £20 per week. He acquired in the course of his duties considerable personal skill and knowledge in regard to the manipulation of the processes and the tanning, dyeing and dressing of skins. About 1929 negotiations were opened with the representatives of a company carrying on a somewhat similar business in New Zealand for the sale of the tanning, dressing

(1) (1874) L.R. 10 Ch. 96.

and dyeing portion of the appellant's business and the equipment connected therewith. The respondent took an active part in these negotiations. The price suggested on the part of the appellant was £8,500 for plant and establishment charges, and £5,500 for the processes and the business as a going concern. But the representatives of the New Zealand company were not prepared to pursue the negotiations unless assured that the respondent would be available to any company or organization that it formed to take over the business. The appellant, through its chairman of directors, intimated that it could not retain the respondent in its service if the portion of its business relating to the tanning, dyeing and dressing of skins were sold, and advised the respondent to make the best deal he could with the new company. The result was that the respondent arranged to join the new company or organization at a salary of £20 per week and a further sum of £5,000, payable partly in shares and partly by promissory notes over an extended period. It was also arranged that his service agreement, as it has been called, should endure for a period of three years, and that the respondent should covenant not to go into competition against the new company or organization for at least five years. Some few days subsequently to this arrangement, negotiations for the purchase of that part of the appellant's business already mentioned were resumed. The respondent took an active part in these negotiations. The representatives of the New Zealand company intimated that the secret or business processes were of no practical use or value without the respondent, whom it had to employ, and suggested a sum of £8,500 for the part of the appellant's business already mentioned, including the secret or business processes. This proposition was discussed by the directors of the appellant, who resolved that the plant, furniture, fittings and formulae be offered to the New Zealand company for £8,500, stock and certain rights to be taken over at cost price. The representatives of the New Zealand company closed with the offer. The respondent was present at the meeting of directors of the appellant company, but he did not then or at any other time disclose the particulars of his service agreement to them or to the shareholders of the company.

H. C. OF A. 1935-1936.

FURS LTD. v. TOMKIES.

Dixon J.

The appellant's case is that the £5,000 payable to the respondent under his service agreement with the new company or organization was for disclosing its secret or business processes, and therefore an illicit gain, acquired in the conduct of the company's business, whilst the respondent denies that the payment was for disclosing any secret or business process and claims that it was for teaching the workmen of the new company or organization how to apply and work the processes acquired or to be acquired by it. The learned Judge who tried the case and heard and saw the witnesses accepted the respondent's version of the facts. The distinction is fine, but it is clear enough : as I understand the learned Judge, the respondent acquired no personal benefit from anything connected with the appellant's processes or business, but merely undertook to impart the personal skill and knowledge acquired by him in the practical working of the secret and business processes. The rule of law above stated is a most salutary one, but it does not preclude anyone from making the most of his own skill and talent and so earning his living. The respondent was entitled to enter the service of the new company or organization, and no one suggested that he was accountable for the salary of £20 per week payable to him under his service agreement. The learned Judge was of opinion that the sum of £5,000 was also remuneration for his personal services and was not an illicit gain acquired in the course of the appellant's business. I should agree with the learned Judge if the facts were as he found them. But unfortunately that finding is contrary to various documents put in evidence. It is possibly consistent with the service agreement, which stipulates that the respondent should serve as consulting technical expert and give the full benefit of his knowledge and experience in the treatment and dressing and dyeing of furs and skins, and in the use of the formulae and chemicals and processes formerly used by him in the conduct of the business of Furs Ltd. or known to him from any source whatsoever ; but the agreement also requires him to make a full disclosure of all information which is then or may thereafter during the currency of the agreement be within his knowledge or power. It is inconsistent with an undertaking given by a representative of the New Zealand company to

the respondent in August 1929 (Ex. 2) to deliver promissory notes for £4,000 as consideration for procuring (*inter alia*) all the appellant's "formulae now used ready for use or in the course of compilation." It is inconsistent with a receipt given by the respondent in January 1930 for promissory notes for £4,000 "as purchase price for dressing and dyeing formulae." It is inconsistent with an agreement of March 1930 (from which the signatures were subsequently torn) describing the respondent as in possession of the formulae and purporting to sell the same. It is inconsistent with a letter of May 1930 (Ex. 5) from a representative of the New Zealand company to the respondent acknowledging the receipt "of the dressing and dyeing formulae instructions and information . . . for the following consideration :—

Cash	£1,000
Four notes . . . payable in 1, 2, 3, and 4 years	4,000
	£5,000 "

The learned Judge regarded these documents as records of a fictitious transaction entered into for the purpose of creating an apparent asset in the new company or organization which it was proposed to form. But the finding is also inconsistent with the following extract from the respondent's own evidence :—

Q. You had agreed with Lumb by virtue of the service agreement to disclose this dressing and dyeing formula to Pratt and Lumb's company ? A. I can only answer in this way "with the consent of Furs Ltd."

Q. Is your answer Yes or No ? A. Yes.

Q. And you had agreed to do that before the question of the price to be paid for the formulae was considered ? A. Not only agreed.

Q. In fact, you had agreed upon that before the question of the price to be paid for the equipment and formulae was considered ? A. There is the practical side.

Q. Never mind about the practical side for the moment. Answer my question. You had agreed upon that ? A. Yes.

Q. And under the agreement you were to make full disclosure of these formulae in exactly the way in which you did make it ? A. Yes.

H. C. OF A. 1935-1936.

FURS LTD. v. TOMKIES.

Starke J.

Q. These are the formulae Ex. M which you drew out for the purpose of the sale from Furs Ltd. to Fur Dressers and Dyers Ltd ? A. Yes.

Q. And they are formulae which were included in the purchase price of £8,500 ? A. Yes.

Q. And they were also the formulae which under your service agreement you were bound to disclose to Pratt and Lumb's company ? A. Yes.

Q. And under the service agreement your obligation was to disclose dyeing in exactly the same detail ? A. Yes.

Q. Would you mind telling his Honor, if you had agreed by your service agreement for £5,000 to disclose these formulae to Pratt and Lumb's company, what value would they have in Furs Ltd.'s hands as an asset for sale to that company, for the same company with whom you entered into the service agreement ? A. They would be decidedly depreciated.

Q. Would there be any value left at all ? A. No.

The finding of the learned Judge cannot, I think, be supported in the face of evidence such as I have related, and this notwithstanding the fact that he saw and heard the witnesses. In my opinion, the evidence establishes, beyond any reasonable doubt, that the respondent used his position as a director for his own personal gain, and obtained the £5,000 for procuring the sale of the appellant's processes and business and for disclosing those processes to the New Zealand company and any organization formed by it.

The appeal should be allowed, and a decree made substantially in the form set forth in the amended statement of claim.

McTIERNAN J. I agree with the judgment of my brothers *Rich*, *Dixon* and *Evatt*, and would add only a reference to some observations of the Vice-Chancellor (Sir *J. L. Knight Bruce*) in *Benson* v. *Heathorn* (1) :—" It is mainly this danger, the danger of the commission of fraud in a manner and under circumstances which, in the great majority of instances, must preclude detection, that in the case of trustees and all parties whose character and responsibilities are similar (for there is no magic in the word), induces the Court (not only for the sake of justice in the individual case, but for the

(1) (1842) 1 Y. & C.C.C. 326, at pp. 343, 344 ; 62 E.R. 909, at pp. 916, 917.

protection of the public generally, and with a view to assert and vindicate the obligation of plain and direct dealing between man and man in all cases, but especially in those where one man is trusted by another) to adhere strictly to the rule, that no profit of any description shall be made by a person so circumstanced—saying, to the person complaining that he has thus employed his time and skill without remuneration, that he has elected so to treat the matter; that he has had his reward, for he has had the possibility, nay the probability, of retaining to himself that which he never ought to have retained; that he has been willing to run the risk, and cannot complain if he happens to lose the stake. It is on this principle that Lord *Eldon* proceeded in the cases so familiar to us all of purchases by trustees. It is only an instance of the application of the rule, not the rule itself. In those cases Lord *Eldon* said (I allude particularly to *Ex parte Lacey* (1), which occurred soon after Lord *Eldon* first received the Great Seal): 'The rule is founded on this, that, though you may see in a particular case that he has not made advantage, it is utterly impossible to examine upon satisfactory evidence in the power of the Court, by which I mean, in the power of the parties in ninety-nine cases out of a hundred, whether he has made advantage or not.' . . . If, in the present case, Mr. Heathorn had openly and directly brought forward the matter before the body of shareholders generally, I consider it possible, if not probable, that he would have been allowed to receive, and would now have been entitled to retain all the sums in question paid for commission. He has not elected to take that open and straightforward course; he has chosen that the matter should be undisclosed, and he must abide the inevitable result."

Appeal allowed. Respondent Tomkies to pay costs of appeal and suit.

Solicitors for the appellant, *Greenwell, Shephard & York.*

Solicitors for the respondent Tomkies, *Norton Smith & Co.*

Solicitors for the respondents other than Tomkies, *John Williamson & Son.*

J. B.

(1) (1802) 6 Ves. 625, at p. 627; 31 E.R. 1228, at p. 1229.