

1999

# Breach of Fiduciary Duty: The Alternative Remedies

Denis S. K Ong

*Bond University*, [denis\\_ong@bond.edu.au](mailto:denis_ong@bond.edu.au)

Follow this and additional works at: <http://epublications.bond.edu.au/blr>

---

This Article is brought to you by the Faculty of Law at [ePublications@bond](mailto:ePublications@bond). It has been accepted for inclusion in Bond Law Review by an authorized administrator of [ePublications@bond](mailto:ePublications@bond). For more information, please contact [Bond University's Repository Coordinator](#).

---

# Breach of Fiduciary Duty: The Alternative Remedies

## **Abstract**

This paper examines the alternative equitable remedies available against fiduciaries who have either made profits or caused loss through their breach of duty, and against those who have knowingly assisted them to breach their duty.

## **Keywords**

fiduciary duties, remedies, constructive trust, account of profits, equitable compensation

## BREACH OF FIDUCIARY DUTY: THE ALTERNATIVE REMEDIES\*

*By Denis SK Ong<sup>+</sup>*

This paper examines the alternative equitable remedies available against fiduciaries who have either made profits or caused loss through their breach of duty, and against those who have knowingly assisted them to breach their duty. In the context of this paper, it is proposed to deal with the following topics:

1. The circumstances that will lead a court to award any one of the following remedies against a defaulting fiduciary or his accessory:
  - (a) a constructive trust;
  - (b) an account of profits; and
  - (c) equitable compensation.
  
2. If a court imposes a constructive trust or, alternatively, orders an account of profits, does the court, in determining the scope of the trust or the extent of the profits to be accounted for, apply the principle which requires accountability for *all* profits, as propounded in *Regal (Hastings) Ltd v Gulliver*,<sup>1</sup> or does the court apply the less stringent principle of requiring accountability only for those profits proportionately derived from the use of the misappropriated trust money where the trust money has been improperly mixed by the trustee with his own money, and the mixed fund has been used to make a profitable investment (the tracing principle), as propounded in *Docker v Somes*?<sup>2</sup>

---

<sup>+</sup> Associate Professor of Law, Bond University.

<sup>\*</sup> An earlier version of this paper was presented by the author on 19 April 2000 at the Supreme Court of Queensland Judges' Annual Seminar.

<sup>1</sup> (1942) [1967] 2 AC 134 n. This obligation to account for *all* of the profits was later modified so as to give to the defaulting fiduciary an allowance in respect of his skill and effort: *Boardman v Phipps* [1967] 2 AC 46.

<sup>2</sup> (1834) 2 My & K 655; 39 ER 1095.

## BREACH OF FIDUCIARY DUTY: THE ALTERNATIVE REMEDIES

3. The problems associated with the imposition of a constructive trust on a business carried on in breach of fiduciary duty.
4. The problems associated with the declaration of an equitable charge over the assets of a business carried on in breach of fiduciary duty.

### Appropriate Remedy

#### Constructive Trust or an Account of Profits?

The courts have yet to articulate consistent criteria for determining whether a fiduciary who has made profits from his breach of duty should be ordered to account as a constructive trustee of those profits or, alternatively, be ordered to account for those profits merely as an equitable debtor. The statement made by the High Court in *Maguire v Makaronis*<sup>3</sup> that '[t]he nature of the case will determine the appropriate remedy available for selection by a plaintiff'<sup>4</sup> is too general to be instructive.

In *Keith Henry and Company Proprietary Limited v Stuart Walker and Company Proprietary Limited*<sup>5</sup> the High Court, with some optimism, attempted to present the constructive trust as the only remedy which should be awarded against a fiduciary who had made a profit from his breach of duty, saying:<sup>6</sup>

...[A] trustee must not use his position as trustee to make a gain for himself: any property acquired, or profit made, by him in breach of this rule is held by him in trust for his *cestui qui trust*. The rule is not confined to cases of express trusts. It applies to all cases in which one person stands in a fiduciary relation to another: ...

A less optimistic perspective was proffered in *Consul Development Pty Limited v DPC Estates Pty Limited*<sup>7</sup> by Gibbs J, who observed:<sup>8</sup>

---

3 (1997) 188 CLR 449.

4 *Ibid*, 467.

5 (1958) 100 CLR 342.

6 *Ibid* at 350.

7 (1975) 132 CLR 373.

8 *Ibid* at 395.

The question whether the remedy which the person to whom the duty is owed may obtain against the person who has violated the duty is proprietary or personal may sometimes be one of the some difficulty. In some cases the fiduciary has been declared a trustee of the property which he has gained by his breach; in others he has been called upon to account for his profits and sometimes the distinction between the two remedies has not, it appears, been kept clearly in mind. ...

Gibbs J was there pointing to the dilemma faced by the courts of whether they should impose a constructive trust or should merely order an account of profits with respect to the profits made by the defaulting fiduciary. The remedy which a court awards will prove to be crucial where the fiduciary becomes bankrupt after the court order is made but before he has accounted to the plaintiff, namely, to the person to whom the fiduciary duty was owed.

If the remedy awarded is a constructive trust of the profits (assuming that such profits comprise identifiable assets so as to enable them to form the subject-matter of a trust), then the fiduciary's supervening bankruptcy will not prejudice the plaintiff. This result follows because property held in trust by a bankrupt is not divisible amongst his creditors.<sup>9</sup> On the other hand, if the remedy awarded is an account of profits, and if the assets of the bankrupt fiduciary are insufficient to discharge his liabilities in full, then the plaintiff, being the unsecured creditor of an equitable debt, will obtain only a proportion of the equitable debt owed to him.<sup>10</sup> Thus, for the plaintiff, a constructive trust of the profits will, where this is possible, be a more secure remedy.

In *Consul*,<sup>11</sup> Gibbs J maintained, *obiter*, that where a fiduciary had made profits from his breach of duty, the appropriate remedy was to order him to render an account of those profits. Gibbs J did not there give any reason for his view that, in such a case, an account of profits would be a more appropriate remedy than the imposition of a constructive trust on those profits. Perhaps Gibbs J should have drawn a distinction between profits in the form of traceable assets and profits in the form of a mere monetary value. If the profits comprise traceable assets in existence at the date of the making of the order, then there does not appear to be any

---

9 *Bankruptcy Act 1966* (Cth) section 116(2)(a).

10 *Bankruptcy Act 1966* (Cth) section 108. See also *Corporations Law*, section 555.

11 (1975) 132 CLR 373, at 395.

## BREACH OF FIDUCIARY DUTY: THE ALTERNATIVE REMEDIES

impediment to the declaration of a constructive trust over those assets in favour of the plaintiff. By contrast, if, at the date of the making of the order, there are no profits in the form of traceable assets, then, the profits being no more than a monetary value, an account of profits appears to be the appropriate remedy. This will be so because there cannot be a trust without trust property,<sup>12</sup> and a mere monetary value is not itself an item of property.<sup>13</sup> There must be trust property even in the case of a constructive trust.<sup>14</sup> If the profits initially comprised traceable assets but were dissipated before the making of the order, then the profits would have been transmuted from traceable assets into a mere monetary value, in which case an account of profits would be the appropriate remedy. In *Cashflow Finance Pty Ltd v Westpac Banking Corporation*<sup>15</sup> Einstein J held that there could be no constructive trust without identifiable trust property.

Suppose a trustee misappropriates \$100,000 of trust money and uses only this sum of money to purchase a block of land in his own name. Suppose that the trustee subsequently sells the land for \$150,000 and receives that sum in the form of a cheque. Suppose further that the trustee uses the cheque to open a bank account in his own name.

If, at the date of the making of the court order, the trustee has not operated that account since it was opened, and therefore still has \$150,000 in it, the court will be able to impose, in favour of the trust estate, a constructive trust<sup>16</sup> on the chose in action of \$150,000 which the trustee has against the bank at common law.<sup>17</sup>

However, if, at the date of the making of the order, the trustee had already withdrawn all of the money from the bank account and had dissipated it, then, there being no traceable assets to form a constructive trust, the trustee will be ordered to pay the trust estate \$150,000 from his own funds. That equitable debt of \$150,000 will comprise \$100,000 by way of equitable compensation for the loss of the misappropriated

---

12 *Commissioner of Stamp Duties (Qld) v Livingston* [1965] AC 694.

13 *Mutual Pools & Staff Pty Limited v Commonwealth* (1994) 179 CLR 155, at 196 (per Dawson and Toohey JJ).

14 *Muschinski v Dodds* (1985) 160 CLR 583, at 614 (per Deane J).

15 Supreme Court of New South Wales (Equity Division), Einstein J, 14 May 1999.

16 *Attorney-General for Hong Kong v Reid* [1994] 1 AC 324.

17 *Foley v Hill* (1948) 2 HLC 28, 9 ER 1002; *In re Diplock* [1948] Ch 465, at 522 (per Lord Greene MR, Wrottesley and Evershed L JJ).

trust money and \$50,000 by way of an account of the profits made by the misuse of the trust money.<sup>18</sup>

When it comes to stripping a fiduciary of his unauthorised gains, the courts have done so either by imposing a constructive trust on those gains or by ordering the fiduciary to account for those gains, namely, by ordering the fiduciary to pay the monetary value of those gains. In *Regal (Hastings) Ltd v Gulliver*<sup>19</sup> the directors of a company, in breach of their fiduciary duty, purchased with their own money shares in another company, being shares in which, but for financial constraints, their own company would have purchased. The directors later sold those shares at a profit. The House of Lords, although the company had sought common law rather than equitable remedies, ordered the directors to account in equity to the company for all of their profits. That purely personal remedy was clearly appropriate because the shares had been sold, so that no constructive trust could have been declared over them. Furthermore, as there was no evidence that the profits made by the directors were then identifiable in specie, no constructive trust could have been declared over those profits either.

The remedy given in *Regal (Hastings)*<sup>20</sup> may be compared with that given in *Industrial Development Consultants Ltd v Cooley*.<sup>21</sup> In *Cooley*<sup>22</sup> the defendant, who was the managing director of a company, had, in breach of his fiduciary duty, resigned from that company so as to obtain for himself a number of contracts which his company was interested in acquiring. The defendant made, and would have continued to make, profits from those contracts. The company brought an action to claim those existing and future profits. Roskill J declared the defendant to be a *trustee* of all the profits made or to be made from his contracts and ordered him to account to the company, presumably as a constructive trustee, for those profits.

If Roskill J was there using the term ‘trustee’ in a loose sense, then the constructive trust which he purported to declare would have been merely

---

18 *Scott v Scott* (1963) 109 CLR 649, at 661 (per McTiernan, Taylor and Owen JJ).

19 (1942) [1967] 2 AC 134 n. See also *Cook v Deeks* [1916] 1 AC 554.

20 *Ibid.*

21 [1972] 1 WLR 443. See also *Timber Engineering Co Pty Ltd v Anderson* [1980] 2 NSWLR 488.

22 *Ibid.*

## BREACH OF FIDUCIARY DUTY: THE ALTERNATIVE REMEDIES

an order to account for profits as an equitable debtor.<sup>23</sup> If so, then the order made by Roskill J in *Cooley*<sup>24</sup> was of the same kind as that made by the House of Lords in *Regal*.<sup>25</sup> However, if by ‘trustee’ Roskill J meant to describe someone who held identifiable property for the benefit of another,<sup>26</sup> then his declaration of a constructive trust over the profits would have been difficult to implement because, at the date of the declaration of the constructive trust, there was no evidence of any existing profits in the form of traceable assets to constitute the subject-matter of the trust. Furthermore, the *future* profits could not have formed the subject-matter of any trust declared to exist at the date of the court order.

The distinction between profits constituted by traceable assets and profits which merely define a monetary value was articulated in the order made by Wilberforce J in *Phipps v Boardman*,<sup>27</sup> an order ultimately affirmed by the House of Lords.<sup>28</sup> In *Boardman*,<sup>29</sup> the two defendants, the solicitor to a trust and a beneficiary under the trust, had obtained company shares for themselves by using information acquired by them in the course of their acting for the trust. They had used their own money to purchase those shares.

Wilberforce J held that the defendants were liable to account, subject to their being paid a liberal allowance for their work and skill in acquiring the shares and in making them profitable. Significantly, the order to account comprised two limbs.<sup>30</sup> First, the defendants were ordered to transfer a proportion of their shares to the plaintiff, who was the beneficiary of 5/18 of the trust estate. The relevant shares, subject to an equitable lien in favour of the defendants to secure the reimbursement to them of the price which they had paid for the shares, represented profits in the form of traceable assets such that, pending the transfer of their legal title to the plaintiff, they would have been held on constructive trust for him. Secondly, the defendants were ordered to pay to the

---

23 *Giumelli v Giumelli* (1999) 196 CLR 101, at 112 (per Gleeson CJ, McHugh, Gummow and Callinan JJ).

24 [1972] 1 WLR 443.

25 (1942) [1967] 2 AC 134 n.

26 *Commissioner of Stamp Duties (Qld) v Livingston* [1965] AC 694.

27 [1964] 1 WLR 993, at 1018.

28 [1967] 2 AC 46.

29 *Ibid.*

30 *Phipps v Boardman* [1964] 1 WLR 993, at 1018.

plaintiff a proportion of the profits yielded by the shares (as distinct from the profits represented by the shares themselves) to reflect the plaintiff's 5/18 share of the trust estate. These other profits (as distinct from those profits represented by the shares which were being held on constructive trust) were a mere monetary value and no trust was declared over them because no trust could have been so declared. Thus, with respect to this monetary value, the defendants were made to account as equitable debtors only, although, with respect to the relevant portion of the shares, they were made to account as constructive trustees.

In the context of the fiduciary's accountability, the distinction between profits in the form of traceable assets and profits in the form of mere monetary value was also illustrated in the High Court decisions of *Birtchnell v Equity Trustees, Executors and Agency Company Limited*<sup>31</sup> and *Furs Limited v Tomkies*.<sup>32</sup> In *Birtchnell*,<sup>33</sup> one of three equal partners breached his partnership agreement by joining with a client of the firm in the business of purchasing and reselling land for profit. The delinquent partner died without having accounted to his partners for their proportion of the profits which were made by him from the land sales. The two other partners sued the deceased partner's executors for an account of their proportion of the profits. The High Court upheld their claim and ordered the executors of the deceased partner to account for two-thirds of the profits, the remaining one-third being the deceased partner's own share. The High Court did not declare a constructive trust over the relevant profits. It is suggested that the High Court did not do so because there was no evidence that those profits were represented in any specific assets. Thus, the remedy given in *Birtchnell* was personal and not proprietary. Remarkably, however, in *Keith Henry and Company Proprietary Limited v Stuart Walker and Company Proprietary Limited*<sup>34</sup> the High Court cited *Birtchnell*<sup>35</sup> as a case where the fiduciary's unauthorised profit was made the subject of a *trust* for the benefit of the persons to whom the fiduciary duty was breached.

---

31 (1929) 42 CLR 384.

32 (1936) 54 CLR 583.

33 (1929) 42 CLR 384. See also *Canadian Aero Service Ltd v O'Malley* (1973) 40 DLR (3d) 371; *Katingal Pty Ltd v Amor* (1999) 30 ACSR 545.

34 (1958) 100 CLR 342, at 350.

35 (1929) 42 CLR 384.

## BREACH OF FIDUCIARY DUTY: THE ALTERNATIVE REMEDIES

By contrast, the remedy given in *Furs Limited v Tomkies*<sup>36</sup> was both proprietary and personal, as distinct from being purely personal. There, the defendant, who was the managing director of the plaintiff company, was instructed by the company to sell a part of its business. The defendant negotiated the sale but failed to disclose to his company that the purchasing company had given him £1000 worth of its fully paid up shares and promissory notes for £4000 to induce him to enter its employment. The plaintiff company brought an action to claim that the shares and the promissory notes belonged to it. The High Court agreed with the plaintiff, and ordered the defendant to transfer to the plaintiff the shares and the promissory notes. It may be inferred that, pending such transfer, the defendant would have held the relevant property on a constructive trust for the plaintiff, because, unless the plaintiff owned the property beneficially before the transfer of the legal title to it, there would have been no basis for the order to transfer such legal title to it. There, it was possible and appropriate to impose a constructive trust because the defendant's secret profit was located in traceable assets. Although the remedy given to the plaintiff in *Furs*<sup>37</sup> was proprietary, it was also personal because, under a trust, a trustee not only holds property for the benefit of another but the trustee is also personally liable to that other.<sup>38</sup>

In *Giumelli v Giumelli*<sup>39</sup> the High Court said that a constructive trust was a term which could be extended so as to describe even a purely personal liability in equity. However, it is suggested that a constructive trust should be a trust *of property*. In *Muschinski v Dodds*<sup>40</sup> Deane J said:<sup>41</sup>

...Viewed in its modern context, the constructive trust can properly be described as a remedial institution which equity imposes regardless of actual or presumed agreement or intention (and subsequently protects) to preclude the retention or assertion of beneficial ownership *of property* to the extent that such retention or assertion would be contrary to equitable principle.

---

36 (1936) 54 CLR 583.

37 *Ibid.*

38 *Giumelli v Giumelli* (1999) 196 CLR 101, at 112 (per Gleeson CJ, McHugh, Gummow and Callinan JJ).

39 (1999) 196 CLR 101, at 112 (per Gleeson CJ, McHugh, Gummow and Callinan JJ).

40 (1985) 160 CLR 583.

41 *Ibid.*, at 614. Emphasis added.

It is suggested that Deane J is correct in so formulating the constructive trust as to make it clear that it is not a purely personal remedy.

Furthermore, to extend the concept of the constructive *trust* to include a purely personal equitable liability either to account for profits or to pay equitable compensation would make it impossible to apply to such a purely personal liability the provision in section 116(2)(a) of the *Bankruptcy Act* 1966 (Cth) that *property* held by the bankrupt *in trust* for another person is *not* divisible amongst the creditors of the bankrupt. How could that provision be applied to protect a beneficiary under a non-proprietary 'constructive trust'? Yet such a beneficiary would literally come under the protection of that provision because a constructive trust is, by definition, a form of trust.

#### **An Account of Profits or Equitable Compensation?**

An account of profits directs the defendant to give to the plaintiff the monetary value of what he has improperly obtained,<sup>42</sup> whereas equitable compensation directs the defendant to restore the monetary value of the loss which he has caused to the plaintiff.<sup>43</sup> It may be noted that both of these two remedies, in contradistinction to the constructive trust, are purely personal remedies. Whether the plaintiff elects to have an account of profits or to have equitable compensation will depend on which of these two remedies will, on the facts of the case, yield to him the greater sum of money.<sup>44</sup> But the plaintiff does have the right to elect between the two remedies if, as a result of the defendant's breach of duty, the defendant has made a profit and the plaintiff has suffered a loss.<sup>45</sup>

Curiously, however, there have been occasions when a plaintiff has elected to claim equitable compensation notwithstanding that an order for an account of profits might well have resulted in the award of a larger sum of money. In *Ferrari v Ferrari Investment (Townsville) Pty Ltd (in*

---

42 *Colbeam Palmer Limited v Stock Affiliates Pty Limited* (1968) 122 CLR 25, at 32 (per Windeyer J).

43 *Nocton v Lord Ashburton* [1914] AC 932; *In re Dawson (decd)* [1966] 2 NSW 211.

44 *Warman International Limited v Dwyer* (1995) 182 CLR 544, at 559 (per Mason CJ, Brennan, Deane, Dawson and Gaudron JJ).

45 *Warman International Limited v Dwyer* (1995) 182 CLR 544, at 562 (per Mason CJ, Brennan, Deane, Dawson and Gaudron JJ).

## BREACH OF FIDUCIARY DUTY: THE ALTERNATIVE REMEDIES

*liq*)<sup>46</sup> the plaintiff company's only two directors discontinued the plaintiff's business (the plaintiff being then insolvent) and immediately afterwards commenced the same type of business (a real estate agency for the letting of property) through another company formed and controlled by them, servicing the same clients which the plaintiff had previously done. The plaintiff, after advancing arguments based on constructive trust, account of profits and equitable compensation against the delinquent directors and the company which the latter controlled, elected to ask for equitable compensation. The majority<sup>47</sup> of the Queensland Court of Appeal assessed the amount of compensation payable to the plaintiff to be the full notional price which a hypothetical willing purchaser would have paid to a hypothetical willing vendor for the goodwill of the business.<sup>48</sup> However, it is not immediately apparent as to why the plaintiff did not elect to combine a claim for a constructive trust over the goodwill with a claim for an account of the profits made from the exploitation of that goodwill, namely, an account of the profits made from the misuse of the trust property, that trust property being the plaintiff's goodwill. Such a combination of remedies would have yielded to the plaintiff a larger sum of money than the sole remedy of equitable compensation, because whereas the notional purchase used in measuring equitable compensation gave the plaintiff only the value of the plaintiff's goodwill immediately before the discontinuance of the plaintiff's business, the combined remedies of a constructive trust and an account of profits would have given the plaintiff not only the value of the plaintiff's goodwill immediately before the discontinuance of the plaintiff's business, but also the profits made by the defendants by their subsequent exploitation of that goodwill. The position of the defendants (the delinquent directors and the company formed by them) was analogous to that of a trustee who had misappropriated trust property *and* who had made profits from the misuse of that property. Since the plaintiff's goodwill was still *traceable*, it is difficult to fathom the plaintiff's decision to sue for equitable compensation, as distinct from suing for a constructive trust to be imposed on the goodwill and for an account of the profits made from the misuse of that goodwill.

---

46 Queensland Court of Appeal (Thomas JA and Shepherdson J; Pincus JA dissenting), 22 June 1999.

47 Thomas JA and Shepherdson J; Pincus JA dissenting.

48 See also *Mordecai v Mordecai* (1988) 12 NSWLR 58.

### Constructive Trust or Equitable Compensation?

In *Royal Brunei Airlines Sdn Bhd v Tan*<sup>49</sup> the defendant had knowingly assisted a trustee (a company of which he was the managing director) to misappropriate and dissipate trust funds. The Privy Council ordered the defendant 'to make good [the] resulting loss'<sup>50</sup> to the beneficiary of the trust (the plaintiff). The order so made was clearly one of equitable compensation. Curiously, however, the Privy Council gave effect to its order by restoring<sup>51</sup> the order made by Roberts CJ in the High Court of Brunei, notwithstanding the Privy Council's view that Roberts CJ had there held that the defendant 'was liable as a constructive trustee'.<sup>52</sup> It was distinctly anomalous for the Privy Council to make an order for equitable compensation by restoring what it described as an order making the defendant liable as a constructive trustee. Perhaps the Privy Council in *Royal Brunei Airlines*<sup>53</sup> was using the term 'constructive trustee' in the same extended sense in which that term was later used by the High Court in *Giumelli*,<sup>54</sup> namely, in the sense of someone who was merely an equitable debtor. Such a purposeless extension of the term 'constructive trustee' should be avoided.

### Regal (Hastings) Ltd v Gulliver *or* Docker v Somes?

Suppose that a trustee misappropriates \$100,000 of trust money and combines this sum of money with \$200,000 of his own money to start a business. The trust estate will have contributed *one-third* of the capital of the business and the defaulting trustee will have contributed *two-thirds* of it. Suppose further that the business is successful and that the net assets of the business have reached \$600,000. A net profit of \$300,000 will thus have been made.

Does the defaulting trustee have to account to the trust estate for the misappropriated trust fund of \$100,000 as well as the *entire* profit of \$300,000 (making a total accountability of \$400,000) or, alternatively, does the defaulting trustee have to account to the trust estate for the

---

49 [1995] 2AC 378.

50 *Ibid* at 392.

51 [1995] 2 AC 379, at 393 (per Lord Nicholls).

52 [1995] 2 AC 378, at 383 (per Lord Nicholls).

53 [1995] 2 AC 378.

54 (1999) 196 CLR 101, at 112 (per Gleeson CJ, McHugh, Gummow and Callinan JJ).

## BREACH OF FIDUCIARY DUTY: THE ALTERNATIVE REMEDIES

misappropriated trust fund of \$100,000 together with *only* that proportion of the profit attributable to the misuse of the trust fund, namely, only *one-third* of the profit of \$300,000, which comes to \$100,000 (making a total accountability of only \$200,000)?<sup>55</sup>

If the first alternative is applied, then the trust estate will acquire the entire profit of \$300,000, so that the trustee is stripped of all of the profits. However, if the second alternative is applied, then the trust estate will merely acquire one-third of the profit, namely, only \$100,000. The second alternative, but not the first alternative, will allow the defaulting trustee to *retain* two-thirds of the profit, namely, \$200,000.

The problem is one of identifying the relevant principle of *causation*. The defaulting trustee will argue that his two-thirds profit of \$200,000 was proportionately derived from the use of his own capital contribution of \$200,000, as against a total capital contribution of \$300,000 and a total net profit of \$300,000. He will argue that the trust estate is merely entitled to a one-third profit of \$100,000 because that was the only profit derived from the use of the trust estate's capital contribution of only \$100,000, as against a total capital contribution of \$300,000.

The trust estate, on the other hand, will argue that *but for* the misappropriation of the trust fund of \$100,000, *no* profit would have been made, so that the *entire* profit was made by virtue of the misuse of the trust fund.

Whose assessment is right, that of the defaulting trustee or that of the trust estate? Judicial decisions are divided on the answer to this question.

If the principle of causation enunciated in *Regal*<sup>56</sup> is applied, then the trust estate will be entitled to the entire profit of \$300,000. On the other hand, if the principle of causation enunciated in *Docker v Somes*<sup>57</sup> (the

---

55 In either case, a deduction will need to be made to pay the defaulting fiduciary an allowance for his skill and effort: *Boardman v Phipps* [1967] 2 AC 46. This will be so even if the defaulting fiduciary was dishonest: *Warman International Limited v Dwyer* (1995) 182 CLR 544.

56 (1942) [1967] 2 AC 134n. See also *Boardman v Phipps* [1967] 2 AC 46.

57 (1834) 2 My & K 655; 39 ER 1095.

tracing principle) is applied, then the trust estate will be entitled to merely a proportion of the profit, namely, to merely \$100,000.

In *Scott v Scott*<sup>58</sup> a trustee, who was also the beneficial life tenant, had improperly used trust money together with his own money to purchase a house in his own name. The house subsequently substantially increased in value. The defaulting trustee restored the misappropriated trust money to the trust estate, but did not account to the trust estate for any part of the increased value of the house. After the death of the defaulting trustee, the new trustee, together with the beneficiaries of the trust, sued the executrix of the defaulting trustee for the entire amount of the increase in the value of the house, namely, for the entire profit made from the purchase of the house.

In the Supreme Court of Victoria, Hudson J rejected<sup>59</sup> the plaintiffs' claim to the entire profit but held that the plaintiffs were nevertheless entitled to that proportion of the profit attributable to the use of the misappropriated trust money. In doing so, Hudson J followed *Docker v Somes*,<sup>60</sup> among other cases. Thus, Hudson J applied the tracing principle, as distinct from the more stringent *Regal*<sup>61</sup> principle. The defendant appealed to the High Court against Hudson J's decision on the ground that the defaulting trustee was liable only to restore the amount of the misused trust fund,<sup>62</sup> which he had done before his death, and that he, and therefore his deceased estate, was not liable to account for any of the profit made by his misuse of that fund. The plaintiffs, however, did *not* cross-appeal against Hudson J's order that the trust estate was entitled to only a proportionate share of the profit, and not to the entirety of that profit. This meant that the High Court was *not* asked by the plaintiffs to decide whether or not the trust estate was entitled to the *entire* profit.<sup>63</sup> So, the High Court was not asked to make a choice between *Regal*<sup>64</sup> and *Docker v Somes*.<sup>65</sup> The High Court dismissed the defendant's appeal and upheld the order made by Hudson J.

---

58 [1964] VR 300 (Hudson J) and (1963) 109 CLR 649 (High Court).

59 [1964] VR 300, at 312-313.

60 (1834) 2 My & K 655; 39 ER 1095.

61 (1942) [1967] 2 AC 134n.

62 The defaulting trustee did not have to pay interest on the misused trust money because he held the sole beneficial life interest in the trust estate.

63 *Scott v Scott* (1963) 109 CLR 649, at 657 (per McTiernan, Taylor and Owen JJ).

64 (1942) [1967] 2 AC 134n.

65 (1934) 2 My & K 655; 39 ER 1095.

## BREACH OF FIDUCIARY DUTY: THE ALTERNATIVE REMEDIES

Nevertheless, although the High Court did not resolve the conflict between the *Regal*<sup>66</sup> principle and the principle in *Docker v Somes*,<sup>67</sup> it did examine the hypothetical situation of a trustee purchasing a parcel of shares with £1,000 of misappropriated trust money and £1,000 of his own money, with those shares later appreciating to £3,000. The High Court concluded, on the facts of its hypothesis, that the trust estate would be entitled to only *one-half* of the entire profit of £1,000, with the defaulting trustee being entitled to the *other half* of that profit, observing:<sup>68</sup>

...[T]here can be no doubt that they<sup>69</sup> would be entitled not only to have the sum originally misapplied made good but also to obtain *one-half* of the resultant profit. ...

Thus, the High Court in *Scott v Scott*<sup>70</sup>, in the examination of its hypothesis, appeared to prefer the principle in *Docker v Somes*<sup>71</sup> to that in *Regal*,<sup>72</sup> notwithstanding that earlier in its judgment<sup>73</sup> it had approved the principle in *Regal*.<sup>74</sup> However, in *Paul A Davies (Australia) Pty Ltd (in liq) v Davies*<sup>75</sup> the New South Wales Court of Appeal awarded to the plaintiff a remedy which could be construed as having resulted from that court's application of the principle of full accountability in *Regal*<sup>76</sup> rather than the principle of proportionate accountability in *Docker v Somes*.<sup>77</sup> But the matter awaits resolution by the High Court. In *Warman International Limited v Dwyer*<sup>78</sup> the High Court, in a joint judgment,<sup>79</sup> cautiously observed:<sup>80</sup>

---

66 (1942) [1967] 2 AC 134n.

67 (1834) 2 My & K 655; 39 ER 1095.

68 *Scott v Scott* (1963) 109 CLR 649, at 662 (per McTiernan, Taylor and Owen JJ). Emphasis added.

69 The beneficiaries of the trust.

70 (1963) 109 CLR 649.

71 (1834) 2 My & K 655; 39 ER 1095.

72 (1942) [1967] 2 AC 134n.

73 (1963) 109 CLR 649, at 658.

74 (1942) [1967] 2 AC 134n.

75 [1983] 1 NSWLR 440.

76 (1942) [1967] 2 AC 134n.

77 (1834) 2 My & K 655; 39 ER 1095. See also *Paul A Davies (Australia Pty Ltd (in liq) v Davies* [1983] 1 NSWLR 440, particularly at 455-459 (per Mahoney JA).

78 (1995) 182 CLR 544.

79 Mason CJ, Brennan, Deane, Dawson and Gaudron JJ.

80 (1995) 182 CLR 544, at 561. Emphasis added.

...[T]he stringent rule requiring a fiduciary to account for profits can be carried to extremes and that in cases outside the realm of specific assets,<sup>81</sup> the liability of the fiduciary should *not* be transformed into a vehicle for the *unjust enrichment* of the plaintiff.

The High Court added:<sup>82</sup>

...[A]s a *general rule*, in conformity with the principle that a fiduciary must not profit from a breach of fiduciary duty, a court will not apportion profits in the absence of an antecedent arrangement for profit-sharing but will make allowance for skill, expertise and other expenses.

By stating that a court's refusal to apportion profits to a defaulting fiduciary was only a *general rule*,<sup>83</sup> and by also stating that the plaintiff must not be *unjustly enriched* at the expense of even a defaulting fiduciary,<sup>84</sup> the High Court was recognising that a court would apportion profits to a defaulting fiduciary where a failure to do so would unjustly enrich the plaintiff, being the person to whom the fiduciary duty was owed.

If a court finds that the application of the *Regal*<sup>85</sup> principle will unjustly enrich the plaintiff, does it mean that the court should then, in favour of the fiduciary, apply the principle of apportionment in *Docker v Somes*?<sup>86</sup> Or should the court adopt an *intermediate* position, and apportion to the fiduciary only such a proportion of the profits as is necessary to avoid unjustly enriching the plaintiff? In other words, should the court, in merely doing what is necessary to avoid the unjust enrichment of the plaintiff, treat the defaulting fiduciary *more generously* than what the *Regal*<sup>87</sup> principle prescribes, but *less generously* than the principle of apportionment upheld in *Docker v Somes*?<sup>88</sup> It is suggested that this question should be answered in the affirmative.

---

81 It is unclear as to why, in principle, such an exception should have been made.

82 (1995) 182 CLR 544, at 562. Emphasis added.

83 *Ibid.*

84 (1995) 182 CLR 544, at 561.

85 (1942) [1967] 2 AC 134n.

86 (1834) 2 My & K 655; 39 ER 1095.

87 (1942) [1967] 2 AC 134n.

88 (1834) 2 My & K 655; 39 ER 1095.

## BREACH OF FIDUCIARY DUTY: THE ALTERNATIVE REMEDIES

Suppose a trustee misappropriates \$100,000 of trust money and combines this sum with \$900,000 of his own money to start a business. Suppose that the business is thriving and its net assets have acquired a value of \$2,000,000. Since the original combined capital was \$1,000,000, the net profit will be \$1,000,000. If the trustee is required to account on the basis of *Regal*,<sup>89</sup> then, although the trust estate contributed only 10% of the capital, it will reap 100% of the net profit. On the other hand, the trustee, who contributed 90% of the capital, will be barred from obtaining any part of the profit. It seems clear that the application of the *Regal*<sup>90</sup> principle to such a situation will unjustly enrich the trust estate at the expense of the defaulting trustee, and that such an unjust enrichment should be prevented.

But is this unjust enrichment of the trust estate to be prevented merely by applying the principle in *Docker v Somes*?<sup>91</sup> If that principle is applied, then the trust estate will obtain only 10% of the net profit and the defaulting trustee will obtain 90% of that net profit. However, such a result will be unjust to the trust estate because it treats the misuse of the misappropriated trust money as if it were an *authorised* investment of that money. Thus, on the assumed facts, to give the defaulting trustee 90% of the net profit is to countenance his breach of trust, which is a step which should not be taken, because to countenance the trustee's breach of trust would be to enrich the defaulting trustee unjustly at the expense of the trust estate.

It is suggested that, on the facts of the hypothesis, the *trust estate* should receive *more than* 10% of the net profit (thereby avoiding the injustice of the rigid apportionment principle in *Docker v Somes*<sup>92</sup>) but it should receive *less than* 100% of the net profit (thereby also avoiding the injustice of the principle which requires the fiduciary to account for the *entirety* of the profits, namely, the *Regal*<sup>93</sup> principle). It is suggested that the defaulting trustee should be given from the *net* profits:

- (i) the full value of the skill and effort which he contributed to the conduct of the business; and

---

89 (1942) [1967] 2 AC 134n.

90 *Ibid.*

91 (1834) 2 My & K 655; 39 ER 1095.

92 (1834) 2 My & K 655; 39 ER 1095.

93 (1942) [1967] 2 AC 134n.

- (ii) only a *part* of that proportion of the *balance* of the *net* profits derived from the use of his own capital, in recognition of the fact that his use of the *trust* money in conjunction with his own money to operate the business was *unauthorised*. If the mixing of the trust money with the trustee's own money had been *authorised*, which is not the case here, then *no* deduction would be made from that proportion of the net profits derived from the use of the trustee's own money, so that, in that event, the entirety of that proportion would be *retained* by the trustee. That proportion of the *balance* of the net profits, as distinct from the amount to be *deducted from* that proportion, is to be measured by the principle of apportionment in *Docker v Somes*.<sup>94</sup> The amount *deducted from* what would otherwise have been the defaulting trustee's proportion of the *balance* of the net profits will depend on the degree of culpability shown in the trustee's misconduct, so that, for example, a fraudulent trustee will have an amount deducted from his proportionate profits substantially greater than the amount which would have been deducted in the case of a non-fraudulent trustee.

However, if the defaulting trustee breached his fiduciary duty and made net profits *without* having used *any* trust property to do so, then he should be given from the *net* profits:

- (i) the full value of the skill and effort which he contributed to the conduct of the business; and
- (ii) only a proportion of the balance of the net profits remaining *after* the deduction from those profits of the full value of his skill and effort. The defaulting trustee should not be given the *entirety* of the balance because to do so would be to overlook his breach of fiduciary duty. The proportion which the defaulting trustee is to receive *from this balance* will depend on the degree of culpability shown in his breach of duty, so that the higher the degree of culpability shown, the smaller will be the proportion of the balance received by him.

---

94 (1834) 2 My & K 655; 39 ER 1095.

## Problems associated with the imposition of a constructive trust on a business carried on in breach of fiduciary duty

In *Hospital Products Limited v United States Surgical Corporation*<sup>95</sup>  
Mason J said:<sup>96</sup>

...I should mention that a particular problem has arisen with respect to the declaration of a *constructive trust* of a competing business established and carried on by a fiduciary in breach of his duty. One approach, *more favourable* to the fiduciary, is that he should be held liable to account as *constructive trustee* not of the entire business but of the particular benefits which flowed to him in breach of his duty. Another approach, *less favourable* to the fiduciary, is that he should be held accountable for the entire business and its profits, due allowance being made for the time, energy, skill and *financial contribution* that he has expended or made. ...[I]t is not possible to say that one approach is universally to be preferred to the other, for each case depends on its own facts and the form of inquiry which ought to be directed must vary according to the circumstances. In each case the form of inquiry to be directed is that which will reflect as accurately as possible the *true measure* of the profit or benefit obtained by the fiduciary *in breach* of his duty.

The statement made above by Mason J was approved by the High Court in *Warman International Limited v Dwyer*.<sup>97</sup> In his statement Mason J purported to apply a principle of causation by confining the accountability of the defaulting fiduciary to such profits as were obtained by him *in breach* of his duty. However, although Mason J required the application of a principle of causation, he did not *identify* the principle of causation which he had in mind.

Thus, Mason J's statement in *Hospital Products*<sup>98</sup> that the fiduciary is required to account for only 'the profit or benefit which the fiduciary has made *in consequence of*<sup>99</sup> his breach of duty leaves completely unanswered the question whether that consequent profit is to be

---

95 (1984) 156 CLR 41.

96 *Ibid*, at 110. Emphasis added. Mason J was there adopting the dichotomy purportedly formulated by Upjohn J in *In re Jarvis decd* [1958] 1 WLR 815, at 820.

97 (1995) 182 CLR 544, at 558.

98 (1984) 156 CLR 41.

99 *Ibid*, at 110. Emphasis added.

measured by the principle of causation applied in *Regal*,<sup>100</sup> or by that which was applied in *Docker v Somes*,<sup>101</sup> or, indeed, by some third principle of causation.

Furthermore, the dichotomy propounded by Mason J in *Hospital Products*<sup>102</sup> comprising an approach ‘*more favourable* to the fiduciary’<sup>103</sup> and a second approach ‘*less favourable* to the fiduciary’<sup>104</sup> is a dichotomy of incompletely formulated alternatives. The approach supposedly more favourable<sup>105</sup> to the fiduciary makes him account as constructive trustee ‘of the particular benefits which *flowed to him* in breach of his duty.’<sup>106</sup> However, the approach so formulated does not *identify* the principle of causation to be applied. It does not indicate whether the ‘but for’ test is to be applied (*Regal*<sup>107</sup>), or whether the test of concurrent causes is to be applied (*Docker v Somes*<sup>108</sup>), or whether some third test of causation is to be applied. The approach so formulated is thus incompletely stated.

The other approach, which is supposedly ‘less favourable’<sup>109</sup> to the fiduciary, is to make him account as constructive trustee ‘for the entire business and its profits, *due allowance* being made for the time, energy, skill and *financial contribution* that he has expended or made.’<sup>110</sup> The reference to due allowance being made for the fiduciary’s financial contribution does not clarify whether that due allowance entitles the fiduciary to receive back merely the amount of his financial contribution (*Regal*<sup>111</sup>), or, alternatively, entitles the fiduciary to receive back the amount of his financial contribution as well as that proportion of the profits ascertained in accordance with the principle in *Docker v Somes*.<sup>112</sup> This means that Mason J’s formulation of the approach which he said was ‘less favourable’<sup>113</sup> to the fiduciary is, similarly to his

---

100 (1942) [1967] 2 AC 134n.

101 (1834) 2 My & K 655; 39 ER 1095.

102 (1984) 156 CLR 41, at 110.

103 *Ibid.* Emphasis added.

104 *Ibid.* Emphasis added.

105 *Ibid.*

106 *Ibid.* Emphasis added.

107 (1942) [1967] 2 AC 134n.

108 (1834) 2 My & K 655; 39 ER 1095.

109 (1984) 156 CLR 41, at 110.

110 *Ibid.* Emphasis added.

111 (1942) [1967] 2 AC 134n.

112 (1834) 2 My & K 655; 39 ER 1095.

113 (1984) 156 CLR 41, at 110.

## BREACH OF FIDUCIARY DUTY: THE ALTERNATIVE REMEDIES

formulation of the supposedly alternative approach, incomplete. Because of the incompleteness shared by both of Mason J's purportedly alternative approaches, it is unclear whether his stated alternatives are in fact alternatives. It may be preferable not to pursue Mason J's purportedly dichotomous approach, and to substitute for that approach a single formula to measure the extent of the defaulting fiduciary's accountability.

Furthermore, in *Warman International Limited v Dwyer*,<sup>114</sup> the High Court did not appear to accept that the *Regal*<sup>115</sup> principle and the principle in *Docker v Somes*<sup>116</sup> were mutually exclusive. In *Warman*,<sup>117</sup> the High Court said:<sup>118</sup>

It is *for the defendant* to establish that it is *inequitable* to order an account of the *entire* profits. If the defendant does *not* establish that that would be so, *then* the defendant must bear the consequences of mingling the profits attributable to the defendant's breach of fiduciary duty and the profits attributable to those earned by the defendant's efforts and investment, *in the same way* that a trustee of a *mixed fund* bears the *onus* of distinguishing what is his own.

The statement made above is not easy to follow. If the defendant, on whom the High Court has placed the onus of proof, does *not* establish that it is *inequitable* to order him to account for the *entire* profits, then, because he has failed to discharge the onus of proof, it will be *equitable* to order him to account for the *entire* profits. However, if the defendant is thereby obligated to account for the *entire* profits, then it makes no sense to give him, when he is already under such an obligation, a concurrent right to prove an entitlement to that proportion of the profits 'attributable to'<sup>119</sup> his efforts 'and investment'.<sup>120</sup>

---

114 (1995) 182 CLR 544.

115 (1942) [1967] 2 AC 134n.

116 (1834) 2 My & K 655; 39 ER 1095.

117 (1995) 182 CLR 544.

118 *Ibid*, at 561-562 (per Mason CJ, Brennan, Deane, Dawson and Gaudron JJ).  
Emphasis added.

119 *Ibid*, at 562.

120 *Ibid*.

If the fiduciary is given the right to prove, and does prove, that a proportion of the profits is attributable to his efforts 'and investment',<sup>121</sup> then he will have established that it is *inequitable* to order him to account for the *entire* profits. But the High Court in *Warman*<sup>122</sup> would, paradoxically, give the fiduciary the right to prove his claim to a proportion of the profits *only when* the fiduciary has failed to prove that he is entitled to *any* proportion of those profits, namely, only when the fiduciary has failed to prove that it would be *inequitable* to order him to account for the *entire* profits. If the fiduciary is obligated to account for the *entire* profits, then there is no scope for any right on his part to prove for a *proportion* of those profits.

### **The problems associated with declaring an equitable charge over the assets of a business carried on in breach of fiduciary duty**

In *Warman International Limited v Dwyer*,<sup>123</sup> Dwyer was the general manager of the Queensland branch of a company called Warman International Limited. The company was the Australian agent for an Italian company which manufactured gearboxes for sale. Dwyer, in breach of his fiduciary duty, persuaded the manufacturer to terminate Warman's agency.

Dwyer also formed two companies as part of his scheme. One of these two companies was owned by Dwyer and his wife jointly, as to one half, and by the Italian manufacturer, as to the other half. This company became the Australian agent for the assembly and sale of the manufacturer's gearboxes. The other company, which was wholly owned by Dwyer and his wife in separate shares, supplemented the agency business of the firstmentioned company. Both companies made profits.

In the Supreme Court of Queensland, Warman sued Dwyer and the two companies for an account of profits and for a declaration that the goodwill of the business of the two companies was held in trust for it.<sup>124</sup> The trial judge (Derrington J) held that Dwyer had breached his fiduciary

---

121 *Ibid.*

122 (1995) 182 CLR 544, at 561-562.

123 (1995) 182 CLR 544.

124 *Ibid.*, at 553.

## BREACH OF FIDUCIARY DUTY: THE ALTERNATIVE REMEDIES

duty to Warman and that the two companies had knowingly assisted him to do so because their controlling minds were aware of, and joined in, Dwyer's breach of fiduciary duty.<sup>125</sup> The trial judge rejected Warman's claim that the goodwill of the business of the two companies was held in trust for Warman,<sup>126</sup> but he decided that Warman was entitled to an account of profits.<sup>127</sup> However, a majority<sup>128</sup> of the Queensland Court of Appeal determined that Warman was not entitled to an account of profits, but was entitled, instead, to equitable compensation for the loss caused to it by Dwyer's breach of fiduciary duty.<sup>129</sup>

The High Court reversed the decision of the Queensland Court of Appeal. The High Court held that Warman was entitled to elect between an account of profits and equitable compensation for the loss suffered by it.<sup>130</sup> The High Court also declared:<sup>131</sup>

[The respondents<sup>132</sup>] must account for the *entirety* of the *net* profits<sup>133</sup> of the businesses before tax *less* an *appropriate allowance* for expenses, skill, expertise, effort *and resources contributed* by them. ...

The High Court clearly ordered a subtraction to be made from the total net profits, so that only the *remainder* of those net profits was payable to Warman (one of the two appellants<sup>134</sup>). The amount subtracted from the total net profits was to be *retained* by the respondents. The *resources contributed* by the respondents were stated to form a part of that subtraction, namely, those resources, and possibly also the profits derived from their use, were to be made an item of allowance for the benefit of the respondents. It may be noted that the High Court in *Warman*<sup>135</sup> used the term 'resources contributed'<sup>136</sup> in contradistinction

---

125 (1995) 182 CLR 544, at 552.

126 (1995) 182 CLR 544, at 553 and 554.

127 *Ibid.*

128 Macrossan CJ and Pincus JA, McPherson JA dissenting.

129 (1995) 182 CLR 544, at 554.

130 (1995) 182 CLR 544, at 562 and 570.

131 (1995) 182 CLR 544, at 568. Emphasis added. See also 570.

132 Dwyer and the two companies which he caused to be incorporated.

133 The period of accounting was for a period of two years from the date on which the relevant company obtained the agency from the Italian manufacturer.

134 The other appellant was *Peko-Wallsend*, being the company which was Warman's undisclosed principal.

135 (1995) 182 CLR 544.

to the words ‘expenses, skill, expertise, effort’,<sup>137</sup> so that by ‘resources contributed’<sup>138</sup> the High Court meant the respondents’ capital contribution only, and not the respondents’ contribution of skill and effort, the latter contribution having been made a separate item of allowance. But the High Court did not declare whether the ‘appropriate allowance’<sup>139</sup> made to the respondents for the ‘resources contributed’<sup>140</sup> by them was to include, not just those resources, but also that proportion of the *profits* derived from the use of those resources.

*First*, if the High Court intended the subtraction from the total net profits to *exclude all* of the *profits* derived from the use of the respondents’ resources, except for such part of those profits as was needed to pay the allowance for the respondents’ skill and effort, then such a result would have unjustly enriched Warman, a result which the High Court might have been expected to reject,<sup>141</sup> although it is unclear whether it did in fact reject such a result. Such a result would have unjustly enriched Warman because, although it would have included an allowance to the respondents for their skill and effort, it would *not* have included any allowance to the respondents in respect of the role played by their *capital* contribution in the production of the net profits.

*Secondly*, the High Court did not intend the subtraction from the total net profits to *include all* of the *profits* derived from the use of the respondents’ resources, because such a result would have unjustly enriched the respondents, given that Warman, not having made any capital contribution to the business conducted by the two respondent companies, would then have received *none* of the net profits.

*Thirdly*, if the High Court had intended that an allowance be made to the respondents in respect of the role played by their *capital* contribution in the production of the net profits, as distinct from that other allowance made to the respondents in respect of the role played by their *skill and effort* in the production of those profits, then the High Court should have propounded a principle to *quantify* the proportion of the net profits to be

---

136 *Ibid.*, at 568.

137 *Ibid.*

138 *Ibid.*

139 (1995) 182 CLR 544, at 568. See also 570.

140 *Ibid.* See also 570.

141 (1995) 182 CLR 544, at 561.

## BREACH OF FIDUCIARY DUTY: THE ALTERNATIVE REMEDIES

*retained* by the respondents pursuant to the firstmentioned allowance. However, the High Court did not propound any such principle. It seems that the order made by the High Court in *Warman*<sup>142</sup> was insufficiently specific as to the relevant principle to be applied.

*Fourthly*, it needs to be emphasised that underlying the order made by the High Court is the difficulty created by the Court's purported requirement that the 'resources contributed'<sup>143</sup> by the respondents be *deducted* from 'the *net* profits'<sup>144</sup> made by them. Such a difficulty exists because the resources contributed by the respondents comprised their contribution of *capital*, and this capital expenditure could only have been deducted from the respondents' *gross* profits, and *not* from their *net* profits.

The High Court ordered that the amounts respectively found due to Warman on the respective net profits made by the two respondent companies should be secured by separate equitable charges over the respective assets of those companies.<sup>145</sup> Any such curial charge, when it is imposed, will, as an equitable charge, be postponed to any previously created *fixed* charge given by the relevant company over its assets. It is assumed that the curial charge itself will be a *fixed* equitable charge, since it does not contemplate any crystallising event.

Three distinct stages should be recognised in relation to the curial charge:

- (i) the accounting period;<sup>146</sup>
- (ii) the period commencing after the end of the accounting period and ending before the imposition of the curial charge; and
- (iii) the period commencing from the date of the imposition of the curial charge.

---

142 (1995) 182 CLR 544, at 568 and 570.

143 (1995) 182 CLR 544, at 568.

144 *Ibid.* Emphasis added.

145 (1995) 182 CLR 544 at 570.

146 This was a period of two years commencing from the date on which the relevant company obtained its agency from the Italian manufacturer.

### **The accounting period**

Because each respondent company was obligated to account to Warman for only the balance<sup>147</sup> of its 'net profits',<sup>148</sup> earned during the accounting period, *all* of the debts, whether secured or unsecured, incurred by each such company during this period will have priority over the equitable debt payable by each such company to Warman. This is so because the *net* profits made during the accounting period can be quantified only after *all* the debts incurred during that period have been fully deducted from the *gross* profits made by the relevant company during that period.

### **The period commencing after the end of the accounting period and ending before the imposition of the curial charge**

The debts incurred during this period, if they are unsecured *and if* they are still unpaid when the curial charge is imposed, will be postponed to the secured equitable debt owed to Warman. However, if any such unsecured debt is nevertheless paid by the relevant company after the imposition of the curial charge, but the creditor thus paid has no notice of the charge at the time of receiving such payment, then that creditor, being a bona fide purchaser of the legal estate for value without notice, will take his payment free of Warman's equitable charge.<sup>149</sup> The weakness in Warman's charge is that, being a charge arising by operation of law, it was not registrable under the *Corporations Law*.<sup>150</sup> The equitable charge given to Warman by the court arose by operation of law because it was not a charge created by the relevant chargor company. Furthermore, the equitable charge given to Warman was also not registrable elsewhere.

### **The period commencing from the date of the imposition of the curial charge**

All debts incurred by each respondent company, whether secured or unsecured, after the imposition of the curial charge, except for those

---

147 This is the balance due to Warman after the deduction, from the company's *net* profits, of the appropriate allowance to be paid to that company.

148 (1995) 182 CLR 544, at 568. Emphasis added.

149 *Pilcher v Rawlins* (1872) 7 Ch App 259, at 268-269 (per James LJ); *Fire Nymph Products Ltd v The Heating Centre Pty Ltd (in liq)* (1992) 7 ACSR 365, at 373 (per Gleeson CJ).

150 *Corporations Law*, section 262(2)(a).

#### BREACH OF FIDUCIARY DUTY: THE ALTERNATIVE REMEDIES

debts which have been tacked onto prior fixed charges, will be postponed to the secured equitable debt owed to Warman. However, once again, Warman's curial charge may prove to be of little practical value because, even with respect to such debts, a creditor who receives payment of his debt from the relevant company without notice of Warman's non-registrable equitable charge<sup>151</sup> will take that payment free of that charge.<sup>152</sup> It is suggested, therefore, that a plaintiff with the benefit of a curial charge should apply to the court for the appointment of a receiver to the defendant company in order to ensure that the postponed creditors of the defendant company are not inadvertently paid in priority to the plaintiff.

---

151 *Ibid.*

152 *Pilcher v Rawlins* (1872) 7 Ch App 259, at 268-269 (per James LJ); *Fire Nymph Products Ltd v The Heating Centre Pty Ltd (in liq)* (1992) 7 ACSR 365, at 373 (per Gleeson CJ).