The Interface Between Contract and Equity

Equity Conference 2023

King's College London

19 December 2023

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1. Introduction

Equity and contract are two of the great intellectual traditions of the common law, using that term in its expansive rather than narrow technical sense. It is important to emphasise that they are traditions. They change over time as social conditions and needs change, and as the understandings of lawyers adapt in the light of those changes.

The common law is itself a sort of overarching tradition, in which Equity and contract are nested. The way these traditions hang together is not a simple matter. Equity has one trajectory and contract has its distinct trajectory. In significant ways they tend to promote different values. For example, in *Norberg v Wynrib* McLachlin J said:

> "In negligence and contract the parties are taken to be independent and equal actors, concerned primarily with their own self-interest. … The essence of a fiduciary relationship, by contrast, is that one party exercises power on behalf of another and pledges himself or herself to act in the best interests of the other. … The fiduciary relationship has trust, not self-interest at its core …"[1]

Moreover, the groups of people who developed the two traditions were often in large part self-conscious participants in them as separate streams of thinking about law and legal problems. Yet these traditions have to be brought into some kind of coherent relationship with each other. As Martin Krygier observes, tradition is inherent in law. This aspect of law allows for change as the tradition is interpreted in modern times, as an authoritative presence from the past. The past speaks with many voices, so choice is necessary to pick out what is authoritative. As Krygier says:

> "Legal traditions provide substance, models, exemplars and a language in which to speak about and within law. Participation in such a tradition involves sharing a way of speaking about the world which, like language though more prescriptively and restrictively than natural language, shapes, forms and in part envelops the thought of those who speak it and think through it".[2]

The origins of both traditions lie in the division between the common law in its narrow and more technical sense and Equity. The common law was born out of a formulary system based on the

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[1] [1992] 2 SCR 226, 272-274.

[2] M. Krygier, "Law as Tradition" (1986) 5 Law and Philosophy 237, 244.

established and time-honoured forms of action. It also tended to favour strict, bright-line rules of property and obligation.[3]

To simplify in a crude and no doubt highly contestable way, Equity as the tradition we know was born in about the fourteenth century and developed out of the jurisdiction of the Lord Chancellors and the judges acting on their behalf to issue specific forms of remedy. This came to be done according to general principles which in turn came to imply certain substantive rights. The Lord Chancellors in the early period operated with considerable freedom to do as they thought was right. This was followed in the nineteenth century by a hardening of the arteries and what is sometimes referred to as the decline of Equity, as it became more an assembly of technical rules.[4]

That is an exaggerated view; and in many ways the tightening of doctrine was a valuable thing. It promoted predictability and stability in the law. Equitable doctrine had to escape Selden's quip about the state of the law depending on the length of the Chancellor's foot. I think there are two particular reasons this became a pronounced feature of the law in the nineteenth century.

First, certain generally accepted moral foundations for how people should behave in using their legal rights began to break down. As is often observed, where there are strong and generally accepted moral norms there is less need for strict law to provide guidance. The appeals of the Chancellors to an ill-defined concept of conscience as the guide for their interventions came to feel less certain.

Secondly, there was the rise of a way of thinking about law as a science in the nineteenth century, in light of the prestige of the natural sciences and Benthamite philosophy. The Treatise tradition was born. Law should be capable of being stated in definite formulae and propositions. Propositions of law were felt to be capable of being worked out like mathematics, with intellectual coherence being a criterion in its own right.[5]

These two factors also underlie the rise of contract as one of the great organising principles of our law. No longer could an appeal to the old forms of action be regarded as a satisfactory way of ordering the law. They left too many questions unanswered and applied in what had come to seem a fairly random way. More intellectual coherence was required to provide predictability.

The scientific approach affected contract as well. The law needed to be stated in clear, generalised propositions. Rather than a law of contracts, a unified law of contract was the desirable model. It was constructed by great judges of the common law in the nineteenth and early twentieth centuries. They had to operate within a more fixed tradition than the Equity lawyers. They were remarkably imaginative, fashioning a new understanding of a coherent unified law of contract out of the rather unpromising raw material of the forms of action and against the background of a rather recalcitrant theory of the common law as the unchanging inheritance given from time out of mind.

The conceptual development of the traditions continued side by side, with lawyers having to be able to cope with the interaction between the two. Lord Reid in his famous lecture in 1972

[3] I. Samet, *Equity: Conscience Goes to Market* (2018, OUP).

[4] P. Atiyah and R. Summers, *Form and Substance in Anglo-American Law: A Comparative Study of Legal Reasoning, Legal Theory, and Legal Institutions* (1987, OUP), 242, 423-424.

[5] S. Milsom, "The Past and the Future of Judge-made Law" (1981-1982) 8 Monash UL Rev 1, 8 ("The appropriation of right and wrong by lawyers led into another process. As enough individual propositions of law became, as it were, explicit, there was the intellectual impulse to fit them together into a system … the end of that was the exposition of substantive rules of law as an object of study for their own sake in text-books").

announced the end of the fairy tale of the declaratory theory of the common law.[6] The result is that there is now a freedom in the development of the common law which more nearly resembles the freedom for development of Equity. This has exacerbated the tension at the interface between Equity and the common law, in particular Equity and contract. If the common law has its own internal powers of adaptation, why does it need a different system of law with distinct rules laid over the top of that? What is it that Equity achieves in the modern law?

Part of the answer to that question lies in the sediment laid down by Equity in the course of its history of interacting with the common law. Equity has established rights, particularly property rights in the field of trust law, which create great flexibility in the management of property and which the legal system cannot do without. Contract law is able to interact with this scheme, such as embedding certain trust obligations within a wider contractual relationship.

Furthermore, Equity has served to obviate the need for an abuse of rights doctrine in the common law. It has thereby allowed the common law freedom to focus on constructing clear, bright-line rules regulating rights between parties, as mapped out in cases such as *Allen v Flood*[7] and *Bradford v Pickles*.[8] We see Equity here imposing some supervening and flexible obligation regarding future conduct, such as a duty to act in good faith or reasonably, to govern the extent to which opportunistic advantage can be taken of express rights when circumstances change in unexpected ways.[9]

When considering the relationship between the common law and Equity in the contractual context, there is a need to engage with the form of the parties' rights.[10] Equitable rights often take the form of rights in relation to other rights. Acknowledgement of this unique structure of equitable rights sheds light on the way they interact with common law rights, on the normative basis for creating them, and on the way one assesses the common law rights against which they arise.[11] An example is the right of a beneficiary of a trust. Where T holds the freehold of land on trust for B, it is T's legal estate, not the land itself, that is the subject matter of the trust. B's right thus has T's right as its subject. In contrast, where O simply holds an unencumbered freehold of land, O's right does not have any other person's right as its subject. Maitland gave an account of how Equity works in this way, and addressed the paradox inherent in the conventional view that a trust involves a split between legal and equitable title. Maitland's solution was to regard the notion of equitable title as, in some important respects, misleading: whilst B's rights under a trust have come to have many of the same practical effects as the rights of an owner,[12] the core technique of Equity in protecting those rights against third parties was to recognise situations where a third party could come under a new duty to B. That protection of B against third parties did not depend on B's having title, in the sense of a property right; rather, the initial obligation of T to B could give rise to a new obligation of a third party to B when interfered with by that third party, so B's protection was in fact the result of a series of personal rights of B.[13] On this view, therefore, it is not possible for

[6] Lord Reid, "The Judge as Law Maker" (1972) 12 JSPTL 25.
[7] [1898] AC 1.
[8] [1895] AC 587.
[9] See Samet (n 3) chapter 2.
[10] See B. McFarlane and R. Stevens, "The Nature of Equitable Property" (2010) Journal of Equity 1.
[11] See B. McFarlane and R. Stevens, "What's Special about Equity? Rights about Rights" in D. Klimchuk, I. Samet and H. Smith (eds.), *Philosophical Foundations of the Law of Equity* (2020, OUP).
[12] F. Maitland, *Equity* ([1909] 2011 ed, CUP) 117.
[13] Ibid., 120.

Equity, as a secondary or supplementary system of legal rules, to contradict the common law position and claim that it is B who is the true owner of the trust property.

Drawing on this perspective in the context of contractual relationships, the contract creates a number of contractual rights under the common law with equitable rules having a specific second-order role to play in determining the extent to which those common law rights may be enforced. In a particular case, the question is whether one party has acquired an equitable right in relation to the common law right of another party. Therefore, it can be observed that contractual rights and fiduciary obligations often operate concurrently. They are both acquired obligations. Each presupposes what Birks calls a "causative event". As Gregory Klass observes:

> "In contract law, the causative event is typically an agreement for consideration. In fiduciary law, the causative event is entering into the right sort of relationship. The claim here is that there is a deep similarity between those causative events, one that illuminates the nature of fiduciary obligations."[14]

This interplay operates throughout the lifecycle of the contract. The relevant form of relationship recognised in some way in Equity (of which trust and fiduciary relationships are paradigms) may arise or subsist in the course of negotiation of a contract, during the performance of the contract, and after the specifically contractual obligations have been terminated.

The contract itself may be of fundamental importance in establishing the relevant equitable relationship and in defining or affecting its terms. Since contract is taken to represent the will of the parties, and consent of a person is taken to provide an especially strong foundation for treating them as subject to legal obligations, the usual position is that contract trumps or at least moulds obligations which have other foundations.[15] In essence, freedom of contract implies that parties are at liberty to create, or attempt to exclude, fiduciary obligations as they see fit. Three situations can arise and are considered below: (i) the contract expressly provides for fiduciary obligations; (ii) the contract states expressly that a party does not owe fiduciary obligations; and (iii) the contract is silent about the nature of the relationship created, but appears to impose at least some obligations which might be said to create a fiduciary relationship between the parties.

2. The contract as the source or determinant of equitable obligations

In category (i), a contract may expressly stipulate that the relationship between the parties is to some extent fiduciary. In such cases, the analysis is often relatively straightforward. Equity's imposition of fiduciary standards can hardly be said to undermine the certainty of the parties' bargain as it is consistent with the express terms of that bargain.[16] Of course, the designation of a fiduciary relationship is only a label: the "law is not merely a matter of definition. Claims that fiduciary relationships are types of contracts or that fiduciary obligations are contractual in nature are not meant to state analytic truths".[17] The scope of the equitable rights and obligations between the parties remains subject to the interpretation of the contract. Equity supplies the criteria for its

[14] G. Klass, "What if Fiduciary Obligations are like Contractual Ones?" in P. Miller and A. Gold (eds.), *Contract, Status, and Fiduciary Law* (2016) chapter 4, 94-95.
[15] See P. Sales, "Contractual Interpretation: Antinomies and Boundaries" in E. Peel and R. Probert (eds.), *Shaping the Law of Obligations* (2023, OUP), chapter 10.
[16] M. Harding, "Equity and the Value of Certainty in Commercial Life" in P. Devonshire and R. Havelock (eds.), *The Impact of Equity and Restitution in Commerce* (2019, Hart Publishing) chapter 7, 149.
[17] Klass (n 14) 94.

application, but those criteria have to be applied in relation to and in light of the contract terms the parties have agreed.

Interpretation of the contract may lead to a finding that an express stipulation that a fiduciary relationship is present is not as broad or as far-reaching as might appear. In *Noranda Australia Ltd v Lachlan Resources NL*[18] clause 14 of a joint venture agreement provided that a party should not negotiate with a prospective assignee of its interest in the joint venture without first notifying the other joint venturers of its intention and giving the other joint venturers a chance to offer to purchase the interest. One of the parties, Geopeko, negotiated the assignment of its interests to Lachlan without first providing the other parties with a chance to purchase its interests. Another party, Noranda, sought to restrain the assignment. Noranda argued that Geopeko had breached a fiduciary obligation contained in clause 7.8 of the agreement. That clause was expressed in broad terms and spoke of the "fiduciary relationship" between the parties.

Although granting the injunction, Bryson J rejected this argument. His Honour held that the agreement had defined the limits of the fiduciary duties owed by Geopeko and that the very general "fiduciary" provision in clause 7.8 did not convert the specific obligation in clause 14 into a fiduciary duty: "it would not be right to impose on the parties fiduciary obligations wider or different to those which in careful terms they imposed on themselves".[19] Such a conclusion seems uncontroversial. The court gave effect to the intentions of the parties as expressed in the contract.

In category (ii), the contract may directly seek to exclude or modify the operation of fiduciary duties. In *ASIC v Citigroup*[20] the exclusion clause in a mandate letter governing advice provided by an investment bank to its client in relation to a proposed takeover was effective to exclude the existence of a fiduciary relationship that would have otherwise existed: "But for the express terms of the mandate letter, the precontract dealings between [the parties] would have pointed strongly toward the existence of a fiduciary relationship in Citigroup's role as an adviser".[21] As Gummow J said in *Breen v Williams*, "a contractual term may be so precise in its regulation of what a party may do that there is no scope for the creation of a fiduciary duty".[22] The contract may exclude the possibility that a fiduciary duty exists.

Specific duties such as duties of skill and care, prudence and diligence may be excluded by clear contract terms, as well as liability for so-called "equitable fraud".[23] Further, particular remedies, or aspects of remedies, may be excluded or limited. For example, in *DHL International (NZ) Ltd v Richmond Ltd*[24] a contract wholly excluded claims of consequential loss. Richardson J for the New Zealand Court of Appeal said that "it is at least arguable that the contractually agreed exclusion of liability for consequential loss should continue to govern any relationship in equity: why should Richmond derive benefits in equity for which it was not prepared to pay in contract?"[25] In *Friend v Brooker*, the Australian High Court emphasised the importance of the parties' "deliberate commercial decision" to incorporate new fiduciary duties owed to the company in substitution for those owed previously.[26]

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[18] (1988) 14 NSWLR 1.
[19] Ibid., 17.
[20] *ASIC v Citigroup Global Markets Australia Pty Ltd (No 4)* (2007) 160 FCR 35.
[21] Ibid., [325] (Jacobson J).
[22] (1997) 186 CLR 71, 132-133.
[23] *Armitage v Nurse* [1998] Ch 241, 250-253.
[24] [1993] 3 NZLR 10.
[25] Ibid., 23.
[26] (2009) 72 ACSR 1, [86].

However, in category (ii) cases the labelling of the relationship by the parties only takes the analysis so far. Ultimately, Equity looks to the substance of the tasks being carried out by the alleged fiduciary and applies its own established criteria in order to determine whether a fiduciary relationship in fact arises. Parties will not be able to avoid Equity's gaze simply by stating in the contract that no fiduciary relationship is created under it.[27] While parties can craft their relationship as they wish, it is the law, and not the parties, that decides what relationship has been created.[28] The question is whether the parties have agreed to what in law is a fiduciary relationship: "even if they do not recognise it themselves and even if they have professed to disclaim it".[29] As the High Court of Australia has said, the parties to a contract cannot deem a relationship between themselves to be something it is not.[30]

A number of issues may arise in category (iii) cases. Where the contract is silent about the nature of the relationship to which it gives rise, Equity again applies its criteria to determine if a fiduciary relationship exists. Where it does, however, the overall structure of the contract may moderate or mould the scope of a party's equitable obligations. In *Hospital Products Ltd v United States Surgical Corporation*, Mason J said:

> "… it is the contractual foundation which is all important because it is the contract that regulates the basic rights and liabilities of the parties. The fiduciary relationship, if it is to exist at all, must accommodate itself to the terms of the contract so that it is consistent with, and conforms to, them. The fiduciary relationship cannot be superimposed upon the contract in such a way as to alter the operation which the contract was intended to have according to its true construction."[31]

Lord Browne-Wilkinson made the same point in *Henderson v Merrett Syndicates*:

> "The existence of a contract does not exclude the co-existence of concurrent fiduciary duties (indeed, the contract may well be their source); but the contract can and does modify the extent and nature of the general duty that would otherwise arise."[32]

Some scholars have suggested that fiduciary duties should be seen as a species of contractual obligation, arrived at by a process of implication.[33] However, in *White v Jones* Lord Browne-Wilkinson explained:

> "The paradigm of the circumstances in which equity will find a fiduciary relationship is where one party, A, has assumed to act in relation to the property or affairs of another, B. … By so assuming to act in B's affairs, A comes under fiduciary duties to B. … the special relationship (i.e. a fiduciary relationship) giving rise to the assumption of responsibility … does not depend on any mutual dealing between A and B, let alone on any relationship akin to contract. Although such factors may be present, equity imposes the obligation

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[27] See M. Leeming, "The Scope of Fiduciary Obligations: How Contract Informs But Does Not Determine the Scope of Fiduciary Obligations" (2009) 3 J Eq 181, 191; Samet (n 3) 144-145.
[28] L. Smith, "Contract, Consent, and Fiduciary Relationships" in P. Miller and A. Gold (eds.), *Contract, Status, and Fiduciary Law* (2016, OUP) chapter 5, 135.
[29] *Garnac Grain Co Inc v H M F Faure & Fairclough Ltd* [1968] AC 1130, 1137.
[30] *Hollis v Vabu Pty Ltd* [2001] HCA 44, [58].
[31] (1984) 156 CLR 41, 97, endorsed by the Privy Council in *Kelly v Cooper* [1993] AC 205, 215, and the House of Lords in *Hilton v Barker Booth and Eastwood* [2005] 1 WLR 567, 575.
[32] [1995] 2 AC 145, 206.
[33] See e.g. J. Edelman, "When Do Fiduciary Duties Arise?" (2010) 126 LQR 302; the literature is reviewed in Samet (n 3) 116-122.

> because A has assumed to act in B's affairs. Thus, a trustee is under a duty of care to his beneficiary whether or not he has had any dealing with him…"[34]

The better view, therefore, is that fiduciary duties arise by imposition of Equity where a particular role has been assumed by the putative fiduciary.[35] In this area, it is not valid to collapse equitable doctrine into contract. Equity imposes fiduciary obligations for reasons which are normatively independent of contract.

However, the fiduciary's obligations fall "to be moulded and informed by the terms of the contractual relationship".[36] On the one hand, the imposition of fiduciary duties where A has assumed to act in relation to B's property or affairs in a contractual context promotes trust and hence encourages B to rely on A, making B more willing to engage in economic activity with A. Conversely, the ability of A, under the principle of freedom of contract, to stipulate the areas within which he undertakes duties of the kind to be regarded as fiduciary, or declines to do so, enhances the willingness of A to act in that role. So also does his ability to limit by contractual exclusion clauses his liability for acting in that role, subject to an honesty limitation.[37]

In category (iii) cases, where the contract is silent regarding the nature of the relationship between the parties, although some terms might indicate the existence of fiduciary obligations, the contract may nonetheless have certain features that meet the demanding test for the implication in fact of a term that switches off any such obligation. As I observed at first instance in *F&C v Barthelemy*:

> "Fiduciary duties are obligations imposed by law as a reaction to particular circumstances of responsibility assumed by one person in respect of the conduct of the affairs of another. As between the parties to a contract, the existence of express or implied contractual terms may be directly inconsistent with the imposition of such duties, and hence exclude them."[38]

As John Lehane observed, where a company's articles empower the director to acquire land for the purposes of its business, according to wide powers of acquisition set out in its memorandum of association, it cannot be the case that the director must make full disclosure to the board in every case before he privately acquires land for himself, where there is no attempt to compete with the company in the pursuit of an opportunity known to be of interest to it.[39] The scope of a fiduciary obligation may be reduced because it is to be implied, as a matter of contract, that the area of conduct to which the fiduciary obligation attaches is smaller than what is covered by the contract's express terms. Thus, in a common scenario where a real estate vendor retains an estate agent in the knowledge that the same agent is acting and intending to act for other vendors, there can regularly be implied a term that the agent is entitled so to do, with the consequence that the agent is authorised to be in a position of conflict, and is not obliged to disclose all material information to *any* of his or her principals.[40]

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[34] [1995] 2 AC 307, 271.
[35] For academic discussion to support this view, see Samet (n 3) 122-151.
[36] *Hilton* (n 31), [30] (Lord Walker).
[37] See the discussion in P. Sales, "Exemption Clauses in Trusts" in P. Davies, S. Douglas and J. Goudkamp (eds.), *Defences in Equity* (2018, Hart Publishing), chapter 7.
[38] *F&C Alternative Investments (Holdings) Limited v Barthelemy and Culligan* [2011] EWHC 1731 (Ch), [225] (Sales J).
[39] J. Lehane, "Fiduciaries in a Commercial Context" in Finn (ed.), *Essays in Equity* (1985, Law Book Company Ltd) 95, 104-105.
[40] See *Kelly* (n 31).

In some cases, an exclusionary implication may be derived from the text of the contract. As mentioned above, in *Noranda* the agreement expressly provided that the parties were fiduciaries.[41] Yet the contract also provided that the agreement should not constitute the parties "an association, corporation, mining partnership or any other kind of partnership and should not constitute the parties partners agents of legal representatives of other parties for any purpose whatsoever".[42] Bryson J proceeded on the basis that at least in some aspects of their venture the parties were subject to fiduciary obligations,[43] yet held that the detailed provisions governing sale of a parties' interest in the joint venture, requiring that each party should have the right to match or better any offer made by a prospective assignee before being required to approve the assignee as a new member of the joint venture, delineated an area of conduct within which fiduciary obligations did not extend. In the exercise of that contractual right, there was no obligation to act other than self-interestedly: "It would not be right to impose on the parties fiduciary obligations wider or different to those which in careful terms they imposed on themselves."[44]

More broadly, the court may look at the contract as a whole to conclude that it would be inconsistent with the commercial bargain made by the parties to read fiduciary obligations into the relationship established by the contract.[45] The touchstone is to ask what obligations of a fiduciary character may reasonably be expected to apply in the particular context, where the contract between the parties will usually provide the major part of the contextual framework in which that question arises. As explained in *F&C v Barthelemy*:

> "… the overall contextual framework created by the contract simply means that it is not appropriate for the law to impose the whole range of possible fiduciary duties or fiduciary duties of particular types in that specific context – in other words, it may be found that the parties could not reasonably expect that some particular duty of a fiduciary character should apply in the context of their particular relationship or in the context of their relationship with a person accepting appointment as a manager or board member."[46]

3. Conduct as the source or determinant of fiduciary obligations in relation to contracts

The determination of the existence and scope of fiduciary obligations can also be influenced by the parties' conduct. As explained by Leeming JA in *Murdoch v Mudgee Dolomite & Lime Pty Ltd (in liq)*:

> "While contract may be and often is the foundation of a status-based fiduciary relationship (such as a deed of trust, a partnership deed or a solicitor's retainer), and the contract is ordinarily the starting point for identifying the scope of the fiduciary obligation, there are cases where the limits of the area within which the fiduciary is not free to act self-interestedly are delineated not by contract but by conduct."[47]

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[41] *Noranda* (n 18) 13.
[42] At clause 2.3, see Ibid.
[43] Ibid., 17.
[44] Ibid., 15.
[45] See the observation by Lord Neuberger writing extra-judicially in "The Stuffing of Minerva's Owl? Taxonomy and Taxidermy in Equity" [2009] CLJ 537, 543; see also *Vercoe v Rutland Fund Management Ltd* [2010] EWHC 424 (Ch), [351]-[352].
[46] *Barthelemy* (n 38) [225] (Sales J).
[47] [2022] NSWCA 12, [87].

The conduct of the parties can be relevant across the entire span of their relationship. A contract may form the centre-piece of their relationship, but there might be non-contractual normative aspects of it in the period before the contract is formed, in the period after the contract has ended, and also in the period when the contract is on foot. A person may become subject to fiduciary duties through dealings in precontract negotiations. Fiduciary obligations may come to be expanded by virtue of the pattern of dealings between the parties after the contract is up and running. Conversely, such obligations may be reduced below the extent of those originally contemplated in the contract if during the execution of the contract the conduct of the parties narrows the area in which it can be said that the criteria for fiduciary responsibility are satisfied. Also, very significantly, fiduciary obligations may survive the termination of the contract, for example when the fiduciary withdraws from a contract in order to take advantage of a corporate opportunity identified while he was a fiduciary. The post-contract relationship is explored further in section 7 below.

On the one hand, there are cases like *Birtchnell v Equity Trustees* to the effect that where parties to a commercial contract have pursued a course of dealing according to which one party has undertaken to act in the interests of the other, Equity may recognise a fiduciary relationship that reflects the conduct involving such an undertaking which has gone beyond what was required by the initial contract.[48] In *Birtchnell* a partnership deed was the source of fiduciary obligations between the partners, but the scope of those obligations was found to have expanded by reference to the actual conduct of the partnership business. In cases such as these, parties strike a contractual bargain, but Equity supplements that bargain because it recognises facts that are distinct from strict performance of the contract itself as normatively salient.

On the other hand, the parties' conduct may also have the effect of reducing the area within which fiduciary obligations would otherwise extend. An example is the Privy Council appeal arising from the appointment by Anthony Hordern of his brother Samuel as executor.[49] Under the 1878 partnership between Anthony and Samuel, the survivor was required to pay to the executor the value of the stock and assets excluding goodwill of the drapery business. Anthony's appointment of his brother inevitably gave rise to a conflict between interest and his duty as executor, but as Lord Shaw said "it is also true that that conflict is brought about entirely by the action of the late Mr Anthony Hordern, who appointed Mr Samuel Hordern his executor in the full knowledge that he would have to exercise on survivance the rights, and come under the obligations, stipulated in regard to the surviving partner by the articles of association."[50] The same reasoning may be seen where a fiduciary is engaged to carry out a task where there is a known conflict of interest: "If there was any conflict, it was of their own making and a decision which was made by them with knowledge of all the facts relevant to the choice of solicitor. It was a fully informed decision."[51]

The same principle underlies Lord Wilberforce's statement in *New Zealand Netherlands Society v Kuys*: "A person ... may be in a fiduciary position quoad a part of his activities but not quoad other parts: each transaction, or group of transactions, must be looked at."[52] Mr Kuys was the voluntary secretary of a nonprofit organisation supportive of the Dutch community in New Zealand. No complaint was or could be made of his running his own insurance and travel agency business, and it was held that likewise, his efforts in establishing a newspaper fell outside the scope of this

[48] *Birtchnell v Equity Trustees, Executors and Agency Co Ltd* (1929) 42 CLR 384, 407-408 (Dixon J).
[49] *Hordern v Hordern* [1910] AC 465.
[50] Ibid., 475.
[51] *Beach Petroleum NL v Kennedy* (1999) 48 NSWLR 1, [467].
[52] [1973] 1 WLR 1126, 1130.

fiduciary obligations to the society. That seems to have been a case where the known and contemplated conduct of the fiduciary in a particular context led to a reduction in the scope of his obligations more generally.

However, the analysis is different where it is the conduct of the fiduciary itself, not contemplated by the party appointing it or understood by the beneficiaries, which is said to reduce or qualify the fiduciary obligation assumed by it. A fiduciary which places itself in a position of conflict without obtaining fully informed consent is required to perform, as best as can be performed, its obligations to all parties, and to pay compensation for loss suffered if that cannot be done.[53] Leeming suggests that in most cases involving the fiduciary's own conduct, the very same conduct which is invoked to reduce the scope of the fiduciary obligation will in fact amount to a breach of duty.[54] He refers to the common example where a partner acquires an interest in the freehold of the leased premises on which the partnership business is conducted. This puts the landlord/partner in a position of conflict of interest, in respect of which fully informed consent has to be obtained. Thereafter, if that is done, the fiduciary obligations imposed upon the landlord/partner will shrink to accommodate his or her new personal interest as landlord.[55]

4. Good faith obligations in contract and trust environments and self-interested conduct

More generally, it is sometimes said that the holder of a power conferred by contract who is required to act in good faith (whether as a result of an express term or by reason of imposition of a fiduciary duty) can never exercise the power in a self-interested way if the power could otherwise be exercised for the benefit of other people, because "good faith" always requires the power-holder to prioritise the interests of these others. However, this is to misunderstand the good faith requirement, which only requires power-holders to make a sincere commitment to the purposes for which the power has been given; but if these purposes include benefitting the power-holder, then exercising the power to produce such an outcome is not necessarily an action in bad faith in the relevant sense.[56] The purposes for which a power can be exercised are derived from the instrument, read in context, and so are determined by the intentions of the parties themselves. As Brown and Rowe JJ put it in the decision of the Supreme Court of Canada in *Wastech Services Ltd v Greater Vancouver Sewerage and Drainage District*, "the purpose of a discretion is *always* defined by the parties' intentions, as revealed by the contract".[57] Hence the limits of the proper purposes doctrine, unlike good faith, are determined by the parties rather than imposed by courts.[58]

It is not uncommon for circumstances to arise which inevitably mean that a trustee put in place pursuant to some contractual arrangement has a personal financial or other interest in some decision to be taken and this should not disqualify him from acting as trustee where he is not responsible for creating those circumstances. For example, Sir Richard Scott V-C in *Edge v Pensions Ombudsman* observed that pension schemes may allow employer or employee representative trustees to exercise their powers in a self-serving way, provided that they act in good faith, and if schemes require employer and/or employee trustees to be appointed then they impliedly authorise

[53] *Moody v Cox and Hatt* [1917] 2 Ch 71; *Hilton* (n 31), 575.
[54] Leeming (n 27) 196.
[55] See, e.g., *Brenner v Rose* [1973] 2 All ER 535.
[56] See C. Mitchell, "Good Faith, Self-denial and Mandatory Trustee Duties" (2018) 32 Trust Law International 92.
[57] (2021) SCC 7, [133] (emphasis in original).
[58] See generally P.S. Davies and P. Sales, "Controlling contract discretions" (2024) 140 LQR 106.

these trustees to do the same thing.[59] In other words, a trustee who has not put himself into the position of having a conflict of interest does not become disqualified from acting just because a situation may come to arise in which his personal interests are also engaged. In *Lehtimaki and others v Cooper*, it was observed that holding that a charity member is a fiduciary does not mean that there may not be matters on which a member can vote which only concern him personally and not the charity.[60]

The logic of this approach can be seen in a number of contexts. In *Dore v Leicestershire CC*,[61] the local authority was the owner of school premises impressed with the relevant trust and was under no obligation to divest itself of that property; it had an obligation as local education authority to continue to ensure that the school could function effectively at the site; and the costs consequences of litigation would potentially have to be met out of public monies, of which the local authority was the steward. In this context, I observed: "The fact that proceedings are brought against a trustee, which inevitably means that he has a personal financial interest in the proceedings because of potential costs consequences, does not disqualify him from acting as trustee nor from considering how to conduct the proceedings taking account of those consequences."[62] In such circumstances, the local authority "was legally bound to have regard to the potential impact of the litigation on the public monies in its care and in no way acted improperly or unlawfully in doing so."[63]

Similarly, in *F&C v Barthelemy* I explained:

> "Depending on the circumstances, the trustee may legitimately consider that his primary responsibility is to continue to act, as the settlor intended he should, rather than to step down to allow someone else, less well-qualified than him, to take over. If that is the case, the trustee's conscience in continuing to act as trustee will not be affected by the fact that an actual conflict of interest has arisen, provided he seeks in good faith to take proper account of the interests to be promoted by the trust alongside his own interests."[64]

Of course, if power-holders are not authorised to exercise their powers in a self-serving way, then any such purported exercise of power will be flawed not only because it is unauthorised, but also because such persons hold their powers in a fiduciary capacity and are therefore subject to the rules which require them to avoid conflicts of interest.[65]

5. Proper purposes and fraud on a power

This focus on the purposes of the power is also evident when looking at the equitable doctrine of fraud on a power. Where the parties to a contract stipulate that one of them is to have a discretion, generally[66] the inference is that they have resorted to this as a mechanism to allow for reasonable

[59] [1998] Ch 512, 538-541, and the authorities cited by him; his decision was affirmed [2000] Ch 602 (CA).
[60] [2020] UKSC 33, [101].
[61] [2010] EWHC 1387 (Ch).
[62] Ibid., [239] (Sales J).
[63] Ibid., [240] (Sales J).
[64] *Barthelemy* (n 38) [230].
[65] J. Hudson and C. Mitchell, "Legal Consequences of the Flawed Exercise of Scheme Powers" in S. Agnew, P. Davies and C. Mitchell (eds.), *Pensions: Law, Policy and Practice* (2020, Hart Publishing) chapter 7, 135-136.
[66] Sometimes it can be said that a term creating a discretion for a party to act in a particular way is used in a particular context to indicate an intention to demarcate an absolute right for that party, unconstrained by any obligation to have regard to or to protect the interests of the other party.

adjustment of their relationship in the face of future changes of circumstances and that they intend there to be some constraint on the exercise of that discretion. These constraints are inherent in the grant of the power, by reference to the purpose for which it has been granted.

In the context of private law, Equity has been looking at this sort of issue for much longer than the common law. *Duke of Portland v Topham*[67] concerned a power to appoint a fund to either or both of the settlor's daughters. The donee of the power executed a deed of appointment which in form gave the whole of the fund to one of the daughters, but this was done pursuant to an arrangement whereby she would only take half the fund for her own use with the other half being invested in the name of the donee, herself and her brother, to accumulate and be distributed as they saw fit later on. The appointment was set aside for fraud on the power. Lord Westbury LC explained the operation of the doctrine:

> "…the donee, the appointor under the power, shall, at the time of the exercise of that power, and for any purpose for which it is used, act with good faith and sincerity, and with an entire and single view to the real purpose and object of the power, and not for the purpose of accomplishing or carrying into effect any bye or sinister object (I mean sinister in the sense of its being beyond the purpose and intent of the power) which he may desire to effect in the exercise of the power."[68]

Later, in *Vatcher v Paull*[69] Lord Parker took the notion of a fraud on a power, but, emphasising the proper purposes strand of reasoning in cases like *Topham*, articulated the doctrine in a way which covers both patent and latent improper purposes:

> "The term fraud in connection with fraud on a power does not necessarily denote any conduct on the part of the appointor amounting to fraud in the common law meaning of the term or any conduct which could be properly termed dishonest or immoral. It merely means that the power has been exercised for a purpose, or with an intention, beyond the scope of or not justified by the instrument creating the power."[70]

He described the paradigm case of fraud on a power as one where "the appointor's purpose and intention is to secure a benefit for himself, or some other person not an object of the power."[71] Lord Parker's formulation of the principle has come closer to treating it as an aspect of interpretation of the legal instrument itself. How is one to tell what is the scope of the power which is being exercised or for what purposes it might be exercised if not through interpretation of the instrument itself?

However, in the Supreme Court decision in *Eclairs Group Ltd v JKX Oil and Gas Plc*[72] Lord Sumption said that the proper purpose rule inherent in the doctrine of fraud on a power and replicated in section 171(b) of the Companies Act 2006 "is not concerned with excess of power by doing an act which is beyond the scope of the instrument creating it as a matter of construction or implication", but rather with "abuse of power, by doing acts which are within its scope but done for an improper reason."[73] The gap between proper interpretation of the contract and a super-added equitable doctrine of fraud on a power is difficult to identify, particularly since the materials

[67] (1864) 11 ER 1242.
[68] Ibid., 1251.
[69] [1915] AC 372.
[70] Ibid., 378.
[71] Ibid.
[72] [2015] UKSC 71.
[73] Ibid., [15].

used to address both questions are the same. The matters referred to by Lord Sumption as relevant to the identification of the proper purposes for which the power might be exercised – inferring the mischief or object at which the power is directed from the express terms, business context and the practical effects which its exercise in a given context will bring about – seem to be the matters to which one would have regard when interpreting the limits inherent in the power in the contractual setting in which it appears.

Where a wide contractual power of this kind is created, it seems a natural inference that the parties intended it should be used for proper purposes within the scope of what the parties contemplated would be acceptable in the context of their ongoing relationship. The power contains these limits within itself; so it is not relevant to apply the restrictive test for implication of terms. Lord Sumption was rightly concerned to reject that as the relevant test; but it seems arguable that in seeking to achieve this he did not need to reject the idea that identifying the proper purposes for which the power might be used was a function of interpretation of the contract. This is likely to be an area of the interface between contract and Equity which will have to be examined more carefully in future.

I have explored this issue in detail elsewhere[74] but the essential point is that it is not clear that there is any need or justification to lay a distinct equitable principle called "fraud on a power" on top of the contractual obligations. If exercise of a power is within the contemplation of the parties to the contract, why should Equity intervene to defeat their expectations? Perhaps the better view is that the former gap between contract interpretation and equitable obligation has now narrowed essentially to nothing. On a common law approach which is less rigid and reified than it was in the eighteenth or nineteenth centuries, there is less need for a distinct body of equitable doctrine laid over the common law to moderate its effects and provide protection against abuse of the rights it otherwise seemed to lay down. Thus, it may be argued that on a proper approach to contractual interpretation, informed by the lessons drawn from the equitable concept of fraud on a power, perhaps one does not need to look beyond the contract itself to locate the limits on a discretionary power.

6. Rectification and contractual interpretation

All that said, there remain areas in which Equity provides a more useful toolbox than ordinary principles of contractual interpretation. One area that draws this out is the tension between the equitable doctrine of rectification and the common law of interpretation of contracts in respect of correcting mistakes in written contracts. In *Chartbrook Ltd v Persimmon Homes Ltd*,[75] Lord Hoffmann suggested that, if the parties were objectively mistaken about the content of the written contract, such that a reasonable person would consider there to be a mistake, rectification could be ordered on the basis of a common mistake even if one of the parties was not, subjectively, actually making a mistake. Such comments were *obiter*, but were applied by the Court of Appeal in *Daventry District Council v Daventry & District Housing Ltd*.[76]

Significantly, *Chartbrook* departs from traditional equitable principle, which stipulates that the parties' subjective intentions are central to a claim for rectification. The broad approach to interpretation favoured in *Chartbrook*, building on Lord Hoffmann's earlier judgment in *Investors*

[74] P. Sales, "Use of Powers for Proper Purposes in Private Law" (2020) 136 LQR 384.
[75] [2009] UKHL 38.
[76] [2011] EWCA Civ 1153.

Compensation Scheme Ltd v West Bromwich Building Society[77] allows for a greater range of mistakes to be corrected by interpretation at common law. This approach has blurred the line between the objective approach of the common law to construction and the more subjective equitable jurisdiction for rectification.[78] It has also threatened to destabilise some of the core functions of the law on interpretation. Sir Richard Buxton observed, "the law of contract, which individuals and businessmen use to regulate their affairs in order to avoid litigation, should place a premium on certainty. Neither *ICS* nor *Chartbroo*k achieve that end".[79]

Further, Paul Davies argues with force that rectification should also be preferred to interpretation because the equitable jurisdiction is better equipped to protect third-party rights whereby equitable relief might be refused if it would prejudice innocent third parties:

> "Third parties may rely upon the 'plain meaning' of a contract, without being aware of the particular factual matrix which indicates that the contractual language in the formal, written document was used by mistake. Such third parties could be readily protected by the court when exercising its discretion to grant equitable relief, but it is unclear how the common law of interpretation can similarly protect third-party rights."[80]

In *FSHC Group Holdings Ltd v Glas Trust Corporation Ltd*[81] the Court of Appeal restored traditional orthodoxy and rejected the objective approach to establishing a common mistake where the parties had not concluded a binding contact before producing the written instrument. After careful consideration of the development of rectification in contract law, Leggatt LJ concluded:

> "… we are unable to accept that the objective test of rectification for common mistake articulated in Lord Hoffmann's obiter remarks in the *Chartbrook* case correctly states the law. We consider that we are bound by authority, which also accords with sound legal principle and policy, to hold that, before a written contract may be rectified on the basis of a common mistake, it is necessary to show either (1) that the document fails to give effect to a prior concluded contract or (2) that, when they executed the document, the parties had a common intention in respect of a particular matter which, by mistake, the document did not accurately record. In the latter case it is necessary to show not only that each party to the contract had the same actual intention with regard to the relevant matter, but also that there was an "outward expression of accord" – meaning that, as a result of communication between them, the parties understood each other to share that intention."[82]

Where the parties only envisage being bound upon signing a contract, the best evidence of their objective intentions is the formal, written document. For that contract to be rectified for common mistake, both parties must have actually made a mistake and the equitable doctrine of rectification is most suitable for undertaking that analysis.

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[77] [1997] UKHL 28.
[78] M. Briggs, "Equity in Business" (2019) 135 LQR 567, 583.
[79] R. Buxton, "'Construction' and Rectification after *Chartbrook*" [2010] CLJ 253, 261. See also *Tartsinis v Navona Management Co.* [2015] EWHC 57 (Comm), [11] (Leggatt J).
[80] P. S. Davies, "Rectification Versus Interpretation: The Nature and Scope of the Equitable Jurisdiction" [2016] CLJ 62.
[81] [2019] EWCA Civ 1361.
[82] Ibid., [176].

Thus, unlike what may be happening in relation to fraud on a power, in relation to the equitable doctrine of rectification Equity and the common law remain distinct and fulfil different normative functions.

7. The non-concurrent termination of fiduciary and contractual relationships

One final issue to consider is the one alluded to in section 3 above, namely the extent to which a fiduciary relationship, established by contract, might continue after that contract has come to an end. A classic example of this is when the fiduciary withdraws from a contract in order to take advantage of a corporate opportunity identified while he was a fiduciary. One cannot necessarily leave a fiduciary relationship in the same way as a contract is brought to an end.[83] For example, for most purposes a director will usually only owe fiduciary duties to their company for the duration of their directorship and they will come to an end upon their resignation or removal. However, some of the duties that arise during the directorship have a continuing effect after the contract has come to an end. These include the duty to avoid conflicts of interest in relation to the exploitation of any property, information or opportunity of which they became aware of when they were a director of the company. In relation to those matters, the director was impressed with fiduciary obligations by virtue of his role but those obligations continue to operate after he leaves that role. There also remains in place a duty not to accept benefits from third parties in relation to anything done or omitted to be done before the person ceased to be a director.

A classic corporate opportunity case is *IDC v Cooley*.[84] Cooley, the managing director of IDC, had been negotiating a contract on behalf of the company, but the third party wished to offer the contract to him personally and not to the company. Without disclosing his reason to the board of the company, he resigned in order to take the contract personally. It was held that he was in direct breach of his fiduciary duty as he had profited personally by use of an opportunity which came to him through his directorship: it made no difference that the company itself would not have obtained the contract. He was accountable to the company for the benefits gained from the contract.

Conversely, there may be circumstances where the contract establishes a fiduciary relationship but also includes provisions that exclude liability for certain breaches of duty. In the exercise of such duties, the contractual relationship between the parties continues in the absence of the rights and obligations that the fiduciary relationship would otherwise entail. There are limits in law to the extent to which an exclusion clause may protect or relieve a fiduciary from liability, but generally there are good reasons to approach the interpretation of such clauses in an objective way, as is done with clauses excluding other types of liability under contract.[85] In *Armitage v Nurse*, the central question was the validity of an exclusion clause in the Trust Deed, exempting the trustee from liability for gross negligence. Millett LJ explained that it was "far too late" to suggest that an exclusion for ordinary negligence was contrary to public policy and that a trust deed should be interpreted like a contract.[86] The exclusion clause effectively switches off the fiduciary relationship

[83] Samet (n 3) 122, citing D. Markovits, "Sharing *Ex Ante* and Sharing *Ex Post*: The Non-Contractual Basis of Fiduciary Relations" in A. Gold and P. Miller (eds.), *Philosophical Foundations of Fiduciary Law* (2014, OUP) chapter 10.
[84] [1972] 1 WLR 443.
[85] For discussion see Sales, "Exemption Clauses in Trusts" (n 37).
[86] *Armitage* (n 23) 254.

in respect of the duties covered by such a clause but the contractual relationship between the parties continues.

An interesting parallel regarding a distinction between the non-concurrence of termination of a status and termination of a related contract arises in employment law. There, a distinction may be drawn between the employment relationship itself (which has certain legal consequences and governs whether someone has the status of employee in the full sense) and the contract out of which that relationship springs. Where an employee refuses to accept a wrongful dismissal by their employer and decides to keep the contract open, according to normal contractual principles, they are not able to sue in debt for their salary during the period the contract is alive but instead are limited to a claim for damages.[87] Jordan English argues that an employer's obligation to pay a salary or wages can be seen as subject to two conditions: (i) substantial performance of the employee's obligations over the period in which the right to payment accrues; and (ii) the continuation of the relationship of employment—a legal relationship, rooted in a social fact, that is distinct from the contract of employment. On this analysis, an employee may have their relationship brought to an end while the contract which was the foundation for that contract continues in place. So in the fiduciary context, a fiduciary relationship may end but the contract which was the foundation for it may continue to have relevant legal effects. Indeed, in some contexts an employee may be a fiduciary in relation to the employer,[88] and although a wrongful dismissal may not affect the contract of employment unless accepted, it does not follow that the employee remains in a relationship of employment with fiduciary responsibilities: "there is nothing to prevent the employer from, effectively though wrongfully, withdrawing from the employee the legal right to act on his behalf in any respect".[89] The employer's vicarious responsibility for the employee's actions may similarly be brought to an end by termination of the employment relationship even though the employment contract continues.

8. Conclusion

The contract tradition and the Equity tradition have moved closer together. Contractual obligation and fiduciary duty are distinct concepts but their operation is often influenced to a significant extent by the interplay between them. A contract creates rights, and on the "rights against rights" model Equity may impose obligations regarding the use or enforcement of those rights (the doctrine of rectification is an example of this). The principle of freedom of contract requires that parties may stipulate precisely what their duties are, and that the law should respect and give effect to their choice. At the same time, the law (in the guise of Equity) imposes obligations which are normatively justified in the context of certain relationships, judged according to its own criteria. These operate as a form of (often very strong) default rules. They may be disapplied by clear contractual agreement, but this may be hard to achieve. Moreover, the equitable rules wrap around a contract like a blanket. Throughout a contract's lifecycle, moving from negotiation, through implementation, to termination and beyond, Equity may supplement what the contract provides. Contractual interpretation has become an increasingly important part of the analysis to determine where Equity's doctrinal boundaries lie (for instance, in relation to the proper purposes doctrine)

[87] This question was expressly left unresolved by the Supreme Court in *Geys v Société Générale* [2012] UKSC 63. This discussion is informed by the analysis by Jordan English in "Employment Contracts, Conditions, and the Relationship of Employment" (2024) 140 LQR (forthcoming).

[88] When they have powers to act on the employer's behalf, for example to negotiate contracts as its agent.

[89] *Automatic Fire Sprinklers Pty Ltd v Watson* (1946) 72 CLR 435, 451.

and what the content of equitable duties might be (whereby equitable duties are moulded by contract). At the same time, enforcing the bargain made between parties under a contract, and determining the remedies to be afforded, must be done consistently with equitable principles that are imposed by law, unless they are displaced. The resulting pattern is not one in which contract has subsumed the role of Equity, but one of a degree of confluence and of significant, though nuanced and subtle, interaction between them.