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Can mere incompetence constitute a breach of fiduciary duty?

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Introduction

Trustees, when given the responsibility of administering a trust, are subjected to a number of duties. These general duties are commonly found within a trust instrument, should one exist. Simultaneously, whilst in office, trustees are required to act with good faith and confidence on behalf of the beneficiaries, giving rise to what is said to be a 'fiduciary relationship'. This relationship bestows upon the trustee another category of obligations, known as 'fiduciary duties'.

This essay will give a brief overview of what seems to be the most reliable definition of a fiduciary and their function within a trust relationship. In addition, it shall identify the fundamental obligations which derive from fiduciary relationships. It will then critically discuss the courts' disinclination to regard mere incompetence as a breach of fiduciary duty. Rather, it will illustrate that the courts are likely to place incompetence under negligence in tort or the breach of a general duty of care, as is evidenced by the common law.

What are fiduciary duties, and what are their functions?

An appropriate starting point is to explore what the obligations under a fiduciary relationship may entail. The English legal system does not have a settled definition for the term 'fiduciary'. That said, a number of relationships have been regarded as fiduciary per se. These include: principal and agent; director and company, solicitor and client; and, in trusts law, trustee and beneficiary.[1] A frequently cited, and therefore reliable, definition is delivered by Millet LJ in *Bristol & West Building Society v Mothew*,[2] who describes a fiduciary as someone who has elected to act for another 'in circumstances which give rise to a relationship of trust and confidence'.[3] Such a definition leaves the situations in which

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[1] Sukhninder Panesar, 'The nature of fiduciary liablity in English law' (2007) 12 Cov. L. J. 1, 2.

[2] *Bristol & West Building Society v Mothew* [1998] Ch 1.

[3] ibid [18].

someone can be defined as a fiduciary open. This has traditionally been the intention of the courts, in order to preserve a malleable definition that can be applied without any restrictive contextualisation on a case-by-case basis.[4]

Similarly, the term 'fiduciary duty' is used in varied contexts within the legal profession. Traditionally numerous duties have been held under the fiduciary umbrella. The Courts have expressed concern with this extensive approach, and have even gone as far as to say that 'the phrase "fiduciary duties" is a dangerous one',[5] with a narrower model of fiduciary duties being offered up by the Court. Again, it is Millet LJ who has provided the relevant direction, stating that 'The distinguishing obligation of a fiduciary is the obligation of loyalty. The principal is entitled to the single-minded loyalty of his fiduciary'.[6]

While courts have offered up numerous facets of this core obligation, it is easier to sum these up under two key fiduciary duties: the duty to avoid conflicts of personal interest and the duty to avoid making any unauthorised profits that may surface when performing one's fiduciary duties. In broad terms, these have been classified as the 'no conflict' and 'no profit' rules. Historically, the courts have recognised the need to interpret these duties strictly.[7] This view has been disseminated in recent precedence, where the courts have ensured that fiduciaries will be held liable even in cases where they were acting honestly and to the best of their ability, without causing fraud or acting in bad faith.[8] A case that illustrates both of these key duties well is *Boardman v Phipps*.[9] Here, a solicitor for a trust fund used his position to become aware of an opportunity that resulted in a sizeable profit for the trust and himself. The Court held that he breached his fiduciary duty not to make any unauthorised profit. Furthermore, having acted in his own interests, he was also in breach of the 'no conflict' rule. The result of this was that all personal profit made by the solicitor was to be held on constructive trust for the beneficiaries.

Can mere incompetence cause a breach?

With the general obligations of a fiduciary established as loyalty and fidelity, the question remains whether mere incompetence can constitute a breach of fiduciary duty. Much like the law of fiduciaries as a whole, there is seemingly no clear answer. It would be appropriate again to start off with what appears to be the leading response in the aforementioned case of *Mothew*. The pertinent issue here was whether a solicitor breached his fiduciary duties when he incompetently neglected to make his client aware of an existing debt, which may have influenced the granting of a mortgage. The Court of Appeal held that there was no breach of fiduciary duty, as the solicitor's conduct was neither intentional nor dishonest. However, there was a breach of duty of care under the tort of negligence. Millet LJ provided the cogent

[4] *Lloyds Bank Ltd v Bundy* [1975] QB 326 [341].
[5] *Henderson v Merrett Syndicates* [1995] 2 AC 145, [206].
[6] *Mothew* (n.2), [18].
[7] *Keech v Sandford* (1726) Sel Cas Ch 61.
[8] *Regal (Hastings) Ltd v Gulliver* [1967] AC 134 (Lord Russell).
[9] *Boardman v Phipps* [1967] 2 AC 46.

statement: ‘a breach of fiduciary obligation, therefore, connotes disloyalty or infidelity. Mere incompetence is not enough. A servant who loyally does his incompetent best for his master is not unfaithful and is not guilty of a breach of fiduciary duty’.[10] Therefore incompetence, which is neither synonymous with disloyalty or infidelity, cannot constitute a breach of any fiduciary obligation. Rather, it is suggested by *Mothews* that such incompetence may be covered under the law of tort, the law of contract, or under the general duty of care.

In the case of *Paragon Finance plc v D B Thakerar & Co,*[11] a firm of mortgage lenders brought an action against two firms of solicitors who had enacted the purchase of particular properties where the borrowers later defaulted on the mortgages. Both solicitors were initially pursued, *inter alia*, for breach of contract and fiduciary duty via negligence. The claim was then amended to fraudulent breach of trust and intentional breach of fiduciary duty in light of unfavourable precedent. Millet LJ upheld the observation of Chadwick J, that it was ‘contrary to common sense’ to treat claims alleging negligence and incompetence as materially similar to claims alleging fraud and dishonesty, adding that there is ‘no sharper dividing line’ between the two.[12] Therefore, it would appear the court has furthered the notion that incompetence itself is not associated with the fiduciary obligation. It is also interesting to note that the case has drawn a link between incompetence and negligence. Sarah Worthington purports that a ‘negligent fiduciary commits a tort, not a breach of fiduciary duty.’[13] Thus, if a fiduciary is incompetent, does this further suggest the resulting breach is, in essence. the tort of negligence?

An alternative view to this has been presented in the case of *Hilton v Barker Booth & Eastwood*.[14] This case was similar to *Mothew* and *Paragon Finance* in that it related to a solicitor’s failure to disclose information that should otherwise have been presented to the claimant. The court concluded that ‘if a solicitor is careless (…) he may be liable to pay damages for breach of his professional duty, but that is not a breach of his fiduciary duty of loyalty, it is simply the breach of a duty of care’.[15] Again, the courts have refused to deduce that a fiduciary’s inadequacy can constitute a breach of fiduciary duty. However, a substantial difference to note here is the fact that the court has opted to refer this as a breach of the duty of care in trusts law, as opposed to a tort of negligence as seen in *Paragon Finance*. This further suggests that the courts do not consider incompetence to be coupled with fiduciary duties. Similarly, this supports the Law Commission’s view that a duty to exercise reasonable care and skill is not a fiduciary duty.[16]

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[10] ibid, [18].
[11] *Paragon Finance plc v D B Thakerar & Co* [1999] 1 All ER 400.
[12] ibid, [418].
[13] Sarah Worthington, ‘Fiduciaries: when is self-denial obligatory?’ (1999) 58 CLJ 500, 502.
[14] *Hilton v Barker Booth & Eastwood* [2005] UKHL 8.
[15] ibid, [29].
[16] Law Commission, *Fiduciary Duties of Investment Intermediaries* (Law Com No. 350, 2014), para 3.13.

Instead, the duty to exercise reasonable care and skill is categorised within the general, statutory duties owed by a trustee.[17] The duty of reasonable care and skill requires a fiduciary to complete their duties to an objective standard; that of a reasonable prudent and careful man. However, as Rebecca Lee notes, the fiduciary obligation of loyalty is not standard-orientated.[18] It merely necessitates a fiduciary's duty not to depart from acting in the beneficiary's interests. In other words, it does not require a particular standard to be met by a fiduciary. If a fiduciary performs negligently, and subsequently breaches their duty of care, one cannot simply infer that that fiduciary has not still acted to the best interest of their beneficiary. Their act could very well be below the competent standard expected, but this does not render the act a disloyal one. Loyalty is not a concept that can be assessed to a standard; a fiduciary either acts in their beneficiary's interests or they do not. Thus, if competence is a concept that requires assessment against a standard, but the fiduciary obligation of loyalty does not, it is difficult to conclude the two are connected. It follows that the concepts of incompetence and fiduciary duty are distinct from one another.

Conclusion

It has proven difficult to obtain a decisive definition of the term 'fiduciary'. As a result, the phrase 'fiduciary duty' has traditionally been applied elastically and, perhaps snowballed, into a dangerously loose term. The judgment of *Bristol & West Building Society v Mothew* sought to amalgamate these accrued applications into a narrower definition. It would appear it has been successful in this, as it remains an often relied upon precedent across the different branches of law where fiduciary duties emerge.

Moreover, the judgment of this case provided a conclusive statement that mere incompetence cannot alone constitute a breach of fiduciary duty. When examining the court's reasoning, it cannot be concluded that a fiduciary's incompetence may be synonymous with disloyalty or infidelity and therefore a breach of fiduciary duty. Subsequent case law and academic opinion appear to emulate this notion, furthering that an incompetent act will fall under either the tort of negligence or the general duty of care and reasonable skill in equity. Nonetheless, one can draw a reliable conclusion that mere incompetence is not enough to constitute a breach of fiduciary duty.

[17] Trustee Act 2000, s.1.

[18] Rebecca Lee, 'Rethinking the content of the fiduciary obligation' (2009) 3 Conv. & P. L. 236, 251.