> first be satisfied, at stage one, that there is good reason to extend time . . . If he is not so satisfied, that is the end of the application and stage two will never arise. If he is so satisfied, then he must go on, at stage two, to a general exercise of a discretion involving a consideration of all the circumstances including the balance of prejudice or hardship.

Therefore, confirmed by *Baly v Barrett (HL)* [1988] NI 368, it was an error in law to treat a factor like balance of hardship as relevant to the question of whether good reason for extension had been shown, since its relevance only arose in stage two.

When it comes to deciding what matters are relevant at stage one and at stage two, the judge applies a general discretion. Both Liu JA and Nazareth V-P agreed that matters relevant at stage two were not necessarily irrelevant at stage one. There was a degree of overlap. For that reason, the justice of the Defendants' case was to be taken into account not only in the exercise of discretion at stage two but the identification of good reason at stage one. But in the specific instance of the present case, justice certainly would not help to transform that which was clearly not good reason into that which was.

Conclusion

The Court of Appeal unanimously accepted the principle of extending the validity of the writ to be that good reason for the extension was of definite essence before the Court could exercise its discretion. Balance of hardship or sympathy was irrelevant to show a good reason.

John R Edwards
Partner
Koo & Partners

Fiduciary Duty

Equitable fiduciary duty of employee – common law duty of fidelity of employee – causation – burden of proof

Hon Litton, V-P, Godfrey and Ching JJA • Judgment dated 6 September 1996

Civil No 211 of 1995

Mr William Stone, QC, instructed by Messrs Deacons Graham & James for 1st, 2nd and 3rd Defendants/Appellants
Mr Michael Thomas, QC and Mr Godfrey Lam, instructed by Messrs Lovell White Durrant for 1st and 2nd Plaintiffs/Respondents

Kishimoto Sangyo Co Limited
Kishimoto Sangyo (HK) Co Limited
v
Akihiro Oba
Leung Hin Yan, Bernett
BOIS Technology Limited

The fiduciary principle is rarely visited by the Hong Kong Court of Appeal. *Kishimoto Sangyo Co Ltd v Oba* is an exception, but unfortunately the decision is chiefly notable for its inadequacies in analysing the relevant law.

The Plaintiffs brought an action against Mr Akihiro Oba, the former managing director of its Hong Kong office, for, *inter alia*, breach of fiduciary duty and breach of the duty of fidelity implied in the employment contract.

In the year before his resignation, Mr Oba was principally responsible for a project whereby Kishimoto acted as the 'middleman' in arranging the supply of LCD manufacturing equipment from Japan to a Taiwanese company, Prime View, for the production of LCD displays.

Prime View intended to install a pilot plant to test the viability of mass production of LCD displays. By April 1993, Mr Oba reported to Kishimoto that Prime View planned to visit Japan in June 1993 to investigate mass production in 1995 and had requested that Kishimoto accompany it.

Soon after two contracts were made for the installation of the pilot plant, Prime View indicated that it looked forward to Kishimoto's continued full support. At this critical moment, Kishimoto decided that the project should be handled by its Taiwanese rather than Hong Kong subsidiary. Mr Oba was displeased with this decision and on 7 July 1993 gave notice to resign, to take effect on 31 October 1993.

In September 1993, before his resignation took effect, Mr Oba acquired BOIS, the third Defendant, with a view to competing with Kishimoto once he resigned. Meanwhile, he lied to Kishimoto that he intended to go into the antique business.

In December 1993, he started contacting Prime View to promote BOIS. By January 1995, Mr Oba, on BOIS's behalf, was on the verge of finalising a contract with Prime View to supply equipment manufactured by suppliers who formerly cooperated with Kishimoto. Kishimoto had lost the cooperation of these suppliers. Kishimoto immediately issued a writ against Mr Oba and BOIS.

Breach of Fiduciary Duty

Kishimoto argued that had it not been for Mr Oba's activities, which were breaches of his equitable fiduciary duty to his employer, it would have had a good chance of obtaining a significant number of contracts for the Prime View production project.

Applying *Canadian Aero Services v O'Malley* (1973) 40 DLR (3d) 371, the trial judge, Barnett J, accepted that Mr

Oba was in breach of his fiduciary duty by diverting Kishimoto's maturing business opportunity in the mass production project.

The Court of Appeal took the rare step of departing from the trial judge's finding of fact and held that when Mr Oba resigned in October 1993, Kishimoto did not have a maturing business opportunity.

According to Litton VP, the production project was at best prospective and embryonic for two reasons: Firstly, the pilot plant was not set up until December 1993, and even if it had been and Prime View had gone ahead with mass production, there was no certainty that Kishimoto would have obtained the relevant contracts; secondly, the suppliers were wooed over because Mr Oba offered better services than could Kishimoto without Mr Oba's expertise.

With respect, neither of those two reasons stand up against existing authority. The first reason – Kishimoto's failure to show a certainty that it would obtain the mass production contracts – is inconsistent with the fact that the court is only asked to protect an opportunity. The second reason – that the prospective business partner preferred the fiduciary to his principal – has not been a relevant consideration in past decisions. In fact, it is often the hallmark of decisions where the fiduciaries are held liable.

Although the opportunity in *Canadian Aero Services Ltd v O'Malley* was a certainty, Laskin CJC did not adopt this as a strict requirement. In *Industrial Development Consultants Ltd v Cooley* [1972] 2 All ER 162, Roskill J considered it immaterial that the chance of the Plaintiff obtaining the contract was no greater than ten per cent.

In *Green & Clara Pty Ltd v Bestobell Industries Pty* Ltd [1982] WAR 1, the fiduciary obtained the contract by offering the lowest tender, but the Plaintiff's tender being the third lowest it could not have obtained the contract anyway.

In *Markwell Brothers Ltd v Diesel* [1983] 2 Qd R 508, the Plaintiff employer only had an 'outside chance' of maintaining a franchise, but nonetheless succeeded in suing for diversion of the franchise.

Of course, the courts have not protected all business opportunities. They have refused to protect the mere hope of a customer making repeat orders after a first order (*Island Export Finance Ltd v Umunma* (1986) BCLC 460). Nor have they protected a 'global opportunity' on the part of a manufacturer and seller of glass fibre tubes to sell to potential buyers in the market (*Balston Ltd v Headlines Filters* [1987] FSR 33).

The opportunity must also be actively pursued. Hence, in *Peso Silver Mines Ltd v Cropper* [1966] SCR 673, it was not held to be a breach of fiduciary duty for company directors to take up an order that the board had decided not to pursue.

The principle that emerges from these cases is that the more specific and developed the opportunity, the more likely it would be held to be a maturing business opportunity. The reason is simple. When a company has successfully developed a specific business opportunity with a potential customer, it enjoys a headstart over other competitors in the market. This makes it particularly tempting for a fiduciary, who has encyclopaedic knowledge of the opportunity and personal contact with the customer, to usurp the opportunity for his or her own benefit. It is precisely against such conflicts of interest that fiduciary law protects.

Hence, while a fiduciary cannot divert specific business opportunities actively pursued by its principal, it remains free to compete fairly by developing on its own initiative, general business opportunities also enjoyed by other competitors in the market. Because of this, there is much to be said for Barnett J's finding that Kishitomo did enjoy a maturing business opportunity.

A pilot project and its subsequent mass production are parts of an overall scheme rather than entirely distinct transactions. Also, even though mass production was at least a year from commencement, Prime View had indicated a clear intention to proceed with the mass production and had specifically invited Kishimoto to accompany its visit to Japan for that purpose. Kishimoto enjoyed at least a headstart over other competitors.

Causation

The Court of Appeal further held that the Plaintiffs failed to establish causation between the alleged breaches and the loss suffered. This was because it held that Kishimoto's failure to obtain the mass production contracts was due to the loss of Mr Oba's expertise, rather than alleged breaches of his fiduciary duty.

Because of the split trial, the issue of causation was not argued at first instance. Neither was it fully argued before the Court of Appeal. Had it been, the Court of Appeal might have been advised that the test for causation for breach of the equitable fiduciary duty was not as strict as that at common law for breach of contract or tort.

Where breach of fiduciary duty is alleged, a long line of precedent indicates that the onus is on the Plaintiff to show that it suffered loss as a result of the breach. What is unclear from decisions on the matter, is the degree of causal connection required to establish breach of fiduciary duty.

A strong line of authority on non-disclosure of conflict of interest by confidential advisers has shown that sufficient causal connection is established where the Plaintiff shows that, with the benefit of hindsight and common sense, the breach of the fiduciary duty was part of a chain of events which led to the loss (*Brickenden v London Loan & Saving Co* [1934] 3 DLR 465). It would not be open to the Defendant to speculate, in the absence of evidence, that the loss would have occurred even if there had been no breach.

This 'plaintiff-friendly' approach has been attributed to the strict and prophylactic nature of fiduciary duties. It appears that a lower burden of proof is required for breach of the core fiduciary duty of loyalty, as opposed to other equitable duties owed by fiduciaries such as the duty to apply money held upon a bare commercial trust in a particular manner (*Target Holding Ltd v Redfern* [1995] 3 WLR 352). The breach of the duty to avoid a conflict of interest alleged in *Kishimoto* would seem to belong to the former category.

Accordingly, the Plaintiffs should

have been able to take advantage of the lower burden of proof. If this had been the case, it would have been more difficult for the Court to dismiss the causation issue on the ground that the absence of Mr Oba's expertise was the cause of the Plaintiffs' loss.

Even if the absence of Mr Oba's expertise from Kishimoto *was* the most proximate cause of its loss, Kishimoto should have succeeded by showing that the breach was *a* cause of the loss. The burden should have shifted to the Defendant to prove that Prime View would not have contracted with Kishimoto even if Mr Oba had not provided an alternative in competition with his former employer.

Alternatively, as loss of chance is a well-recognised item of loss in claims for breach of fiduciary duty, Kishimoto could have argued that had it not been for Mr Oba's competition in breach, Kishimoto would at least have had a chance of obtaining the contract that Mr Oba was about to sign with Prime View. Because of the split trial, however, the evidence necessary for determining whether such a chance existed, was not led. The most appropriate course might have been to have remitted the matter to the High Court for further hearing on the issue of causation.

Breach of Duty of Fidelity

The Court of Appeal held that Mr Oba, by acquiring BOIS during the period of his employment with a view to competing with Kishimoto (and lying about his future intention), had breached his implied common law duty to act in good faith towards his employer.

This finding in *Kishimoto* is in contrast with a strong line of recent authority for the proposition that by secretly carrying out preparatory acts to set up a business in competition with their employers, employees do not breach their duty to their employers (*Balston v Headline Ltd*).

The decision in *Kishimoto* also sits uncomfortably with the Court's ruling that, on the same facts, there was no breach of fiduciary duty. It is bemusing that the common law duty of fidelity forbids a resigning manager from secretly preparing for his future, while the equitable fiduciary duty of loyalty justifies this as his entitlement to 'cultivate his own commercial relationships ... without attracting the disapproval of equity'.

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Shipping Counterclaims

Admiralty law – whether counterclaims caught as 'actions' under section 8 of Maritime Conventions Act – discretion of court to extend time limit under s 8

The Owners of the Ship or Vessel 'Kafur Mamedov'
v
The Owners and/or Demise Charterers of the Ship or Vessel 'Goldpath' and Others

Hon Nazareth, V-P, Godfrey JA and Seagroatt J • Judgment dated 12 July 1996

Ref: Civil Appeal No 44 of 1996

Mr Michael Thomas, QC and Mr Godfrey Lam, instructed by Messrs Crump & Co for the Appellants
Mr Joseph Fok instructed by Messrs Richards Butler for the Respondents

The Court's strict observance of time limits for the bringing of proceedings often causes grief to plaintiffs but relief to defendants.

In a recent case before the Hong Kong Court of Appeal involving a collision between the vessels *Kafur Mamedov* and *Goldpath*, however, it was the Defendants (Appellants) which sought an extension of the two-year time limit for the bringing of a 'counterclaim' under s 8 of the *Maritime Conventions Act* 1911 (the Act).

The Facts

On 23 August 1993 the *Kafur Mamedov* and the *Goldpath* collided in Hong Kong waters. On 22 August 1995 (the last day before the claim would have been time-barred) the owners of the *Kafur Mamedov* (the Respondents) commenced proceedings against the owners of the *Goldpath* (Appellants). In December 1993 the Appellants filed notice of a counterclaim to the Respondents' claim even though the Respondents were yet to file and serve their statement of claim. The Appellants then issued two motions for extensions of time under s 8 of the Act which provides that '... no action shall be maintainable to enforce any claim ... unless proceedings therein are commenced within 2 years ...'

Section 8 also provides the Court with a general jurisdiction to extend the time limits for bringing proceedings and a specific jurisdiction to extend time where it has not been possible to arrest the Defendant's vessel during the 2-year period.

The trial judge, Waung J., was of the opinion that the Defendants had conceded that s. 8 of the Act applied to Defendants issuing counterclaims in the same way that it applies to Plaintiffs issuing proceedings, and so the issue of whether a counterclaim was an "action" with s. 8 of the Act was not canvassed at first instance.

Waung J denied the application for the extension of time, however, on the ground that s 8 should be applied with some strictness. He observed that: