

Secret profits and semiconductors

What can an employer do if it finds out a senior employee is using his or her position within its organisation to secretly profit from the business the employer undertakes? This was the question recently considered by the Scottish Court of Session. The decision provides some useful tips for employers on what to do when there is a conflict between the actions of an employee and the employer's best interests. In the event a potential conflict is proven, the case also illustrates how the employer can go about clawing back any of the profits earned by the employee.

The facts

This case involved Mr Docherty who was employed by Samsung Semi-Conductor Europe Limited. Samsung imported and distributed semi-conductor products. Mr Docherty's role was to supervise quality assurance in respect of these products.

Unknown to Samsung, Mr Docherty also held a 50% shareholding in a company, DKV, that was engaged by Samsung to provide quality control services.

For a number of years, Mr Docherty used his position within Samsung to ensure Samsung continued to do business with DKV. When one of Samsung's customers decided to move its operations to continental Europe, Mr Docherty provided misleading information to Samsung to persuade it to not to use a competitor to DKV in the new jurisdiction. He then set up a subsidiary to DKV in the jurisdiction so it could continue to do business with Samsung.

Samsung subsequently uncovered Mr Docherty's relationship with DKV and issued proceedings against him, seeking an account of profits (i.e. all the profits he had made from his interest in DKV during the course of his employment with Samsung). Samsung claimed that Mr Docherty owed a fiduciary duty to the company and, through his actions, had breached this duty by allowing a conflict of interest to arise between his involvement in DKV and his responsibilities towards Samsung.

The decision

The Court held that Mr Docherty did owe Samsung a fiduciary duty. This was due to the level of responsibility and influence he enjoyed within Samsung. He was in a position to recommend DKV for work and others would take decisions based on his recommendations. The fact that Samsung did not expressly specify that he was a fiduciary to Mr Docherty did not matter, given he must have been aware of his influential role.

The Court went on to find that there was a potential conflict between Mr Docherty's fiduciary duty and his interest in DKV. As a result he was liable to pay to Samsung an amount equal to the monies he had received from his interest in DKV (which amounted to over €340,000).

Impact

It is worth noting that, as a decision of the Scottish Court of Session, this case is not binding on the English courts, but will still be highly influential. It is also a useful decision for employers.

The case demonstrates an employer does not need to rely on express contractual terms specifying the employee is a fiduciary. Instead the Court will look at the reality of the employee's position within the employer and whether the employee is aware of the influence of his role (which clearly in most cases he should be).

The Court also made clear that an employee who has breached a fiduciary duty can be required to account for the profits which the employee has derived from the wrongdoing. It is not necessary to show that the employer has suffered equivalent loss. The case emphasises that the employer's sanctions are not limited to sacking the wrongdoer, but stripping the profits of the wrongdoer too.

Clearly this will take careful planning, since when an employee is challenged, the wrongdoer may take steps to hide assets, destroy evidence and generally cover their tracks. So it is important to consider the later steps that the employer may wish to take, before taking the first step.

Recommendations

Notwithstanding the points made by the Court above, our view is that it is still worth having an express provision in contracts of employment of senior employees making clear the employer views them as a fiduciary (in addition to the usual confidentiality and restrictive covenant clauses). If an employee has signed up to such a provision, this may be of some persuasive value to the Court.

In the event a Court finds an employee does not owe fiduciary duties, it is also prudent to ensure that contracts contain a clause requiring employees to disclose any outside interests or activities which may conflict with their role.

On a wider note, in light of the forthcoming Bribery Act 2010, employers should also have policies in place for their workforce regarding anti-corruption and bribery.

If you have any questions about any of these issues raised in this legal update, please contact:

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