

## How faithful does an employee have to be?

The Court of Appeal has just decided a case involving the scope of an employee's duties of loyalty and good faith, and also the potential to imply fiduciary obligations into a contract of employment. This is a major decision, with significant practical effects on the drafting of employment contracts, affecting all senior and, we consider, mid-tier employees. This is a useful reminder of the need to update employment contracts when employees are promoted to more senior levels.

The facts of *Ransom v Customer Services PLC* are very simple. Mr Ransom was a senior employee but not a statutory director. He had a short and very basic contract of employment which had not been updated since his early days with the Company. He wished to leave and go into competition, and had two meetings with business contacts prior to his leaving date. The main part of the claim, by the time it reached the Court of Appeal, concerned whether he was in breach of any contractual duties in failing to report what he had done, or whether due to his senior position, he was in breach of any fiduciary duties.

The Court of Appeal took the opportunity to try and resolve confusion in this area, which arises from similar terminology (i.e. duty of good faith versus duty of fidelity versus fiduciary duties). This is often a key issue, because an employer looking to challenge a departing employee at a senior level will often want to identify a breach of a fiduciary duty. Generally, it is felt that if fiduciary duties exist, it is significantly more difficult for an employee prior to departure to undertake any legitimate preparation for competing after departure. Fiduciary duties will often create a duty on the individual to report his own breaches of contract. In addition, a breach of a fiduciary duty may allow the employer to apply for an account of profits, without the employer showing that it has actually lost out as a result. This can be extremely helpful if a customer has moved business to the former employee's new business, and states that it would never have given the business to the old employer.

In the *Ransom case*, the Court of Appeal drew a clear distinction between employees and directors. Fiduciary duties for a director arise because the individual is a director. Fiduciary obligations for employees (who are not also directors) would only arise if it was consistent with the contract and governed by the rules of that contract. There is an implied duty of fidelity, contained in contracts of employment, but again, this is dependent on the terms of the contract of employment itself. The employee may have promised to serve faithfully, but it is important to establish what the employee has promised to do, and to establish whether or not the employee has acted faithfully.

This case means that, if the employer wants to argue that an employee (as opposed to a director) was under a duty to report his own breaches, this could only happen if the contract of employment supports the existence of such an obligation either by express term, or such an obligation is consistent with other terms in the contract, albeit not explicitly set out.

The overall result is that employers should be reviewing their contracts of employment for more senior staff to ensure that the contract gives the employer the protection they require. At the end of the day, the old employer lost, in this case, because it had not upgraded Mr Ransom's very basic contract since he had joined the employer. In the past, it has been argued that fiduciary obligations can be implied for an employee in a senior position. This approach is now shown to be incorrect. For a non-director, fiduciary duties only exist if they are explicitly set out in the contract or are generally consistent with the contract's other terms.

Therefore, for employees at a senior level, employers need contracts which contain express reporting obligations on an employee to report all matters which are of concern to the employer or to impose any other contractual duty equivalent to a fiduciary duty. In that way, the contract of employment will be consistent with the imposition of fiduciary duties. Properly drafted, we

think these provisions should not be seen as threatening, and doubtless, for most employees, they will remain irrelevant because they will honour the contracts and the issue will never come up.

The same approach applies to those who are members of LLPs, where, again, our view is that the contract will need to be consistent with fiduciary duties in order for those to be implied by a court.

If you have any questions, please contact:

***Nicholas Robertson***

T: +44 20 3130 3919

E: [nrobertson@mayerbrown.com](mailto:nrobertson@mayerbrown.com)

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