Implied duties of good faith, fidelity and fiduciary duties

In our previous article “Beyond the Four Walls of the Employment Contract – Good Faith, fidelity and Fiduciary Duties” published on 28 March 2012, we highlighted the existence of implied terms in employment contracts with reference to the Singapore High Court decision in *Smile Inc Dental Surgeons Pte Ltd v Lui Andrew Stewart* [2011] SGHC 241. This decision has since been upheld by the Singapore Court of Appeal in *Smile Inc Dental Surgeons Pte Ltd v Lui Andrew Stewart* [2012] SGCA 39 (“Smile Inc”). In the recently issued judgment, the Court of Appeal has prescribed clearer principles of law on the implied duties of good faith, fidelity and fiduciary duties in the employment context. This update aims to provide an overview of the principles expounded by the Court on the implied duties of good faith, fidelity and fiduciary duties.

The facts and the decision

In Smile Inc, the Appellant, Smile Inc Dental Surgeons Pte Ltd, employed the Respondent, Dr Lui as an associate dentist. While still in the employment of Smile Inc Dental Surgeons Pte Ltd, Dr Lui incorporated his own company, Dental Essence Pte Ltd (“Dental Essence”). A month after incorporating Dental Essence, he resigned from Smile to commence his own business in a location which is within 5 minutes’ walk from Smile’s clinic. Thereafter, Smile experienced a decrease in monthly revenue in respect of the branch at which Dr Lui worked prior to his resignation. Many of Smile’s patients subsequently requested for their dental records and left to become patients of Dental Essence. Smile brought an action alleging that Dr Lui had breached both the express restrictive covenants set out in his employment contract as well as his implied duties of good faith and fidelity and fiduciary duties.

The High Court held that the absence of a time limit in the restrictive covenants rendered them void and unenforceable, on the basis that they were unreasonable in reference to the interests of the parties. This was upheld by the Court of Appeal.

The High Court also held that Dr Lui did not owe any fiduciary duties due to the nature of his role.

In addition, Dr Lui did not breach any implied duties of good faith and fidelity by which he was bound, as he merely took preparatory steps in setting up a competing business while he was still being employed. The Court of Appeal subsequently upheld the High Court’s findings.

The distinction between the duties of good faith and fiduciary duties

In reviewing the High Court’s decision, the Court of Appeal examined the law on the duties of good faith and fiduciary duties in the employment context. The Court of Appeal clarified that there is a distinction between the duties of good faith and fiduciary duties, even though both duties of good faith and fiduciary duties may arise out of an employer-employee relationship.

The Court of Appeal referred to the case of *Man Financial (S) Pte Ltd (formerly known as E D & F Man International (S) Pte Ltd) v Wong Bark Chuan David* [2008] 1 SLR(R) 663 (“Man Financial”) where it was held that “It is trite law that there is an implied term in the employer’s favour that the employee will serve the employer with good faith and fidelity, and that he or she (the employee) will also use reasonable care and skill in the performance of his or her duties pursuant to the employment contract.” It is thus eminently clear from the case of Man Financial that duties of good faith and fidelity will exist in every employer-employee relationship.

On the other hand, fiduciary duties will not arise out of the mere fact that there is an employment relationship. The Court of Appeal cited the English High Court decision of *Nottingham University v Fishel* [2000] IRLR 471 (“Fishel”) and clarified that fiduciary duties “result from the fact that within a particular contractual relationship there are specific contractual obligations which the employee has undertaken which have placed him in a situation where equity imposes these rigorous duties in addition to the contractual obligations.”

Fiduciary duties

The question of whether an employee owes
The implied duty of good faith and fidelity prohibits an employee from competing against the employer during the course of employment. In Smile Inc, the Court of Appeal reaffirmed the position that mere preparatory steps taken to compete with the employer during the course of employment will not constitute a breach of the implied duty of good faith and fidelity, while actively competitive activities would constitute a breach.

It is also pertinent to note that the Court of Appeal had emphasized that whether the steps taken by an employee would constitute a breach of the implied duties of good faith and fidelity is fact sensitive in every case. Consequently, the line between mere preparatory steps and active competitive activities may not be clear.

In this regard, the Court of Appeal shed some light by referring to a number of previously decided cases where the employee’s acts were found to have formed actual competitive activities constituting a breach of the implied duty of good faith and fidelity. Such instances included:

- Acquiring the business of the employer's direct competitor and conducting business using the acquired company;
- Undertaking highly skilled work for a direct competitor of the employer during the employee’s spare time;
- Actively procuring the breakdown of the relationship between the employer and the employer’s principal and accepting the offer of employment from the principal to compete with the employer;
- Soliciting the employer’s customers and/or the employer's employees to join a company incorporated by the employee to compete with the employer, and
- Entering into agreements with actual and potential customers.

An employee’s acts which have previously been held to be merely preparatory activities and consequently permissible include the following:

- Forming an intention to start a competing business;
- Consulting accountant and lawyers on the viability of the competing business;
- Approaching a bank for financing;
- Leasing premises for the competing business;
- Applying and obtaining government grants for the competing business; and
- Writing to the employer’s suppliers to inform them of the intention to start a business and enquiring details of the suppliers' products.

In applying these principles to the facts of the case, the Court of Appeal found that Dr Lui, by incorporating a company, leasing and fitting out the business premises and encouraging another former employee to join the competing business, had merely engaged in preparatory
steps. Accordingly, there was no breach of his implied duties of good faith and fidelity.

**Conclusion**

While employers commonly bring an action against a former employee based on the express restraint of trade and non-solicitation clauses contained in their employment contract, the case of Smile Inc has provided helpful clarification as to the scope of claims based on an employee’s implied duties.

Smile Inc also serves as a reminder of the differences in the scope of express covenants and implied terms in an employment contract. The Court of Appeal pointed out that while express restrictive covenants in the employment contract govern the employee’s conduct after their employment, the implied duties governs the employee’s conduct during his course of employment vis-à-vis his employer. The content of the implied duties are governed by common law.

As such, Smile Inc is a significant decision in helping employers to understand the basis of an action against an employee or former employee.

If you wish to have further information on this update or wish to discuss how it may potentially have an impact on your business, please feel free to contact the following:

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