

Multiple Loyalties and the Conflicted Fiduciary

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Fiduciary loyalty is usually understood as implying an exclusive claim held by the beneficiary over the exercise of fiduciary power by a fiduciary. The beneficiary is said to have a right that the fiduciary exercise fiduciary power exclusively in her interest. The fiduciary is said to be subject to a correlative duty to act solely in the interests of the beneficiary in acting on a fiduciary power. Fiduciary loyalty so understood is a jealous form of partiality—a conception largely, but not entirely, accurate. It captures the typical case in which the conduct of the fiduciary is constrained by proscriptive rules. But it ignores cases in which proscriptive rules must be held in abeyance because the fiduciary acts under an authorized conflict. Conflicted fiduciaries unsettle conventional wisdom about fiduciary loyalty. Supposing that a conflicted fiduciary cannot be expected to be exclusively partial to her beneficiary, in what sense can she nonetheless be expected to be partial to the beneficiary? Can a conflicted fiduciary have multiple but undivided loyalties? If so, how does the conflicted fiduciary prove her loyalty? Once the standard of conduct is determined, what remedies are available? In light of the Supreme Court of Canada’s recent decision in Sun Indalex Finance, LLC v United Steelworkers, the author addresses these and other questions. He establishes a “demonstrable partiality standard” of loyalty, derived from previous cases involving conflicted fiduciaries, to guide a conflicted fiduciary’s actions. The author then analyzes the use of constructive trusts as a remedy for breach of fiduciary duty. He refines the test for determining the availability of a constructive trust and highlights the limits of its use in these situations.

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Introduction

Fiduciary liability is ordinarily conceived of in terms of duties, particularly the duty of loyalty. Whatever else a fiduciary may be compelled by law to do as a fiduciary, she is obligated to be loyal to her beneficiary.¹ We do not often speak of a right to loyalty, but no one could seriously doubt that in a typical fiduciary relationship the duty of loyalty is held subject to a correlative-claim right.² We say that fiduciaries are to be loyal *to their beneficiaries* rather than to be loyal in general³ and that beneficiaries have a legitimate expectation of loyalty *from their fiduciaries*

1. For the nature of fiduciary liability and the Supreme Court of Canada's approach to fiduciary duties and relationships, see Paul B Miller, "A Theory of Fiduciary Liability" (2011) 56:2 McGill LJ 235.

2. For further discussion on correlative rights and duties in law and morality, see Michael Thompson, "What Is It to Wrong Someone?: A Puzzle About Justice" in R Jay Wallace et al, eds, *Reason and Value: Themes from the Moral Philosophy of Joseph Raz* (New York: Oxford University Press, 2004) 333; Stephen Darwall & Julian Darwall, "Civil Recourse as Mutual Accountability" (2011) 39:1 Fla St UL Rev 17. For further discussion on the difference between claim rights and other kinds of rights, especially liberty rights, see Wesley Newcomb Hohfeld, "Some Fundamental Legal Conceptions as Applied in Judicial Reasoning" (1913) 23:1 Yale LJ 16. I speak of "typical fiduciary relationships" in recognition of atypical fiduciary relationships in which the fiduciary is acting for a purpose and without an actual, identifiable beneficiary.

3. Some suggest that a disposition to be loyal in circumstances that warrant loyalty should be considered a virtue. See Iris Samet, "Fiduciary Loyalty as Kantian Virtue" in Andrew S Gold & Paul B Miller, eds, *Philosophical Foundations of Fiduciary Law* (Oxford: Oxford University Press, 2014) 125 [Samet, "Fiduciary Loyalty"].

(but not necessarily anyone else). This is just a circumspect way of saying that by virtue of the relationship between them, the fiduciary has a duty to be loyal to the beneficiary, and correlatively, that the beneficiary has a right to the fiduciary's loyalty. Beneficiaries stand on this right to loyalty when they sue fiduciaries for breach of fiduciary obligation.

The beneficiary's right to the fiduciary's loyalty is in the nature of a claim-right, but otherwise the nature of the right is unclear. Loyalty is a protean concept, often analyzed in terms of equally protean concepts such as trust, fidelity, faithfulness, good faith and altruism.⁴ That being said, the right to loyalty is commonly understood as being an *exclusive* claim enjoyed by the beneficiary over the exercise of discretionary power by a fiduciary.⁵ The beneficiary is *exclusively* entitled to the benefit of the fiduciary's exercise of fiduciary powers and the fiduciary is correlatively obligated to exercise his powers in the interests of the beneficiary alone. Consequently, fiduciary loyalty is widely considered to be an especially demanding sort of partiality.⁶

The exclusive character of the beneficiary's right to loyalty is reflected in standard accounts of the content of the fiduciary's correlative duty of loyalty.⁷ The duty of loyalty is widely understood as encompassing

4. See e.g. Peter Birks, "The Content of Fiduciary Obligation" (2000) 34:1 Israel LR 3; Leo E Strine Jr et al, "Loyalty's Core Demand: The Defining Role of Good Faith in Corporation Law" (2010) 98:3 Geo LJ 629; Matthew Harding, "Trust and Fiduciary Law" (2013) 33:1 Oxford J Leg Stud 81.

5. I have argued this elsewhere. See Paul B Miller, "Justifying Fiduciary Duties" (2013) 58:4 McGill LJ 969 [Miller, "Justifying Fiduciary Duties"]. See also *Bristol and West Building Society v Mothew*, [1996] EWCA Civ 533, [1998] Ch 1 [*Mothew* cited to Ch]. Millett LJ stated, "[t]he distinguishing obligation of a fiduciary is the obligation of loyalty. The principal is entitled to the *single-minded loyalty* of his fiduciary". *Ibid* at 18 [emphasis added]. See also *R v Neil*, 2002 SCC 70, [2002] 3 SCR 631, Binnie J (approvingly citing Henry Brougham's famous expression of lawyerly fidelity in his opening statement of defence of Queen Caroline against the charge of adultery brought by her husband, King George IV: "An advocate, in the discharge of his duty, *knows but one person in all the world, and that person is his client*" at para 12 [emphasis added]).

6. For further discussion on loyalty, partiality and the relationship between them, see generally Simon Keller, *The Limits of Loyalty* (Cambridge, UK: Cambridge University Press, 2007); Simon Keller, *Partiality* (Princeton: Princeton University Press, 2013).

7. By content of the duty I mean the standard(s) of conduct through which compliance with the duty is measured. I take no position here on the question of whether the content of duties includes things other than standards of conduct.

several proscriptive rules.⁸ These rules provide specific expression to the general expectation that fiduciaries will consider only the interests of their beneficiaries.⁹ They stipulate the obligation in a negative fashion, detailing standards of conduct that require the fiduciary to avoid acting, or to avoid situations where she might be tempted to act, other than in the interests of the beneficiary. The most prominent of these rules are the no-conflict rules, which require a fiduciary to avoid conflicts of interest and conflicts of duty.¹⁰ The conflict of interest rule requires the fiduciary to avoid actual or potential conflicts between her own interests and those of the beneficiary. The conflict of duty rule requires the fiduciary to avoid undertaking mandates to serve the interests of distinct beneficiaries,

8. See Matthew Conaglen, *Fiduciary Loyalty: Protecting the Due Performance of Non-Fiduciary Duties* (Portland: Hart Publishing, 2010) at 39–40.

9. The negative character of the proscriptive rules has led some to question whether they are properly to be understood as standards of loyalty. See Lionel Smith, “The Motive, Not the Deed” in Joshua Getzler, ed, *Rationalizing Property, Equity and Trusts: Essays in Honour of Edward Burn* (London, UK: LexisNexis UK, 2003) 53 [L Smith, “Motive, Not the Deed”]. The no-conflict rules do not *seem* to express an expectation that fiduciaries be loyal in the sense of being partial to the interests of their beneficiary. The rules appear to do little more than require that fiduciaries suppress self-interest and avoid conflicting allegiances. I emphasize appearances here because the proscriptive rules may be understood in a manner consistent with the view that true loyalty entails partiality. Here, I wish only to emphasize that the proscriptive rules supply default standards by which a fiduciary’s liability for disloyalty is judged. This is the sense in which I have said, elsewhere, that “the disloyal fiduciary . . . is the conflicted one”. Paul B Miller, “Justifying Fiduciary Remedies” (2013) 63:4 UTLJ 570 at 607. See also Andrew S Gold, “The Loyalties of Fiduciary Law” in Gold & Miller, *supra* note 3, 176 [Gold, “Loyalties”].

10. For present purposes, I define conflicts as follows: a situation in which pursuit or protection of the apparent interests of one party is inconsistent with, or inimical to, pursuit or protection of the apparent interests of another. A *possible* conflict of interest is a situation in which the apparent interests of the relevant parties *may be reasonably foreseen* to conflict in the future but which do not presently conflict. An *actual* conflict is a situation in which the apparent interests of the relevant parties are presently in conflict. A *latent* conflict is a possible conflict that is inherent in a situation given factual or legal incidents of relationships between the relevant parties, the environment in which their interests will be pursued or protected, or the manner in which their interests will be pursued or protected. A *ripened* conflict is an actual conflict rooted in a latent one. Conflicts may be avoided as a result of changes in the interests of the parties, changes in the worldly circumstances in which they are (or were) interested, or through identification of decision options in which the incompatibility of interest between the parties is resolved.

or classes of beneficiaries whose interests do, or may, conflict.¹¹ The proscriptive rules secure the exclusivity of the beneficiary's interest in the execution of a fiduciary mandate by forbidding the fiduciary from considering the interests of others in the mandate. Taken together, the proscriptive rules express an *exclusive-interest* standard of loyalty. The fiduciary who wonders about the basis upon which she may exercise her powers is effectively instructed: "Consider only the interests of your beneficiary; act in your own interest or for the sake of others at your peril."

The prominence of the proscriptive rules fosters two misconceptions about the duty of loyalty. The first is that the right to loyalty is invariably exclusive. That is, the rules suggest it is essential to the nature of the right that it take the form of a sole and undivided claim upon the exercise of a fiduciary's discretionary power. The second is that the content of the correlative duty is defined exclusively or necessarily in terms of avoidance of conflicts.¹² On this view, a fiduciary is actionably disloyal only when he is conflicted, and he is invariably disloyal whenever he is conflicted.

To better understand why these are misconceptions, we must consider contexts in which the duty of loyalty cannot manifest itself as a requirement to abide by an exclusive claim. Think of fiduciary relationships in which the beneficiary is a group of persons (e.g., beneficiaries of a fund) or a personified organization (e.g., a corporation). The right to loyalty generated by these relationships is not an exclusive claim in which the interests of a beneficiary are individuated. Instead, the right is held relative to common interests (e.g., interests in the performance of a fund, or the profitability of a corporation).

11. *Mothew*, *supra* note 5 at 18–19.

12. This view has achieved orthodoxy in Australian fiduciary jurisprudence as a result of Australian High Court decisions. See especially *P & V Industries Pty Ltd v Porto*, [2006] VSC 131. Justice Hollingsworth stated:

The decisions in *Breen* and *Pilmer* clearly confirm that, in Australia, fiduciary duties are limited to proscriptive duties of loyalty. . . . This means that the no conflict and no profit rules encompass the whole content of fiduciary obligations and the duty of loyalty imposed on the fiduciary is promoted by prohibiting disloyalty rather than by prescribing some positive duty.

Ibid at para 23. See also *Breen v Williams*, [1996] HCA 57; *Pilmer v Duke Group Limited*, [2001] HCA 31. This view is also defended at length by Conaglen, *supra* note 8 at 59–76.

It is also instructive to consider circumstances in which the fiduciary is, from the outset of the fiduciary relationship, authorized to act in the face of a known conflict. Partners, for example, are invariably conflicted in that they have a personal interest in the business of the partnership that may conflict with the interests of their co-partners.¹³ Other fiduciaries may be permitted to undertake two or more fiduciary mandates that may conflict. For example, lawyers may be authorized to represent two parties with potentially conflicting interests in a case or transaction.¹⁴ In these circumstances, conflicts are tolerated rather than proscribed and the beneficiary's right to loyalty is not in the nature of an exclusive claim.

Cases where the right to loyalty is not exclusive raise difficult theoretical and practical problems. The core theoretical problems are those of determining the content of the duty of loyalty when the proscriptive rules are held in abeyance, as well as the precise extent to which those rules are held in abeyance. These theoretical issues have real world implications. Importantly, uncertainty about standards of conduct will make it difficult for fiduciaries to recognize and respect the fidelity conditions under which fiduciary mandates are to be executed.¹⁵

These issues are well illustrated in *Sun Indalex Finance, LLC v United Steelworkers*, a recent decision of the Supreme Court of Canada.¹⁶ In *Indalex*, the Court faced the challenge of articulating standards of loyalty applicable to employer-administrators. Employer-administrators are inherently conflicted fiduciaries. As administrators, they are obligated to act in the interests of their employees when administering employee pension funds. As managers of a business, they are obligated to act in the best interests of the company. The mandates of plan administration and business management are evidently distinct and clearly may conflict. Nevertheless, the conflict is authorized. Which raises the question: By what standard of loyalty is a conflicted fiduciary, such as an

13. See generally Larry E Ribstein, "Are Partners Fiduciaries?" [2005] 1 U Ill L Rev 209.

14. For critical discussion, see Richard A Epstein, "The Legal Regulation of Lawyers' Conflicts of Interest" (1992) 60:4 Fordham L Rev 579; Anthony Duggan, "Solicitors' Conflict of Interest and the Wider Fiduciary Question" (2007) 45:1 Can Bus LJ 414.

15. This uncertainty is reflected in the deep differences of opinion and debate over the practical import of rules governing lawyers' conflicts. See Richard F Devlin & Victoria Rees, "Beyond Conflicts of Interest to a Duty of Loyalty: From *Martin v. Gray* to *R. v. Neil*" (2005) 84:3 Can Bar Rev 433.

16. 2013 SCC 6, [2013] 1 SCR 271 [*Indalex* SCC].

employer-administrator, to be governed? How is the conflicted fiduciary to responsibly handle conflicts when they ripen? Furthermore, what remedy would be appropriate when the duty of loyalty is breached?

In this article, I address these and other questions in light of *Indalex*. In Part I, I summarize the case. In Parts II, III and IV, I critically analyze the reasons given in *Indalex*. In Part II, I argue that *Indalex* does not provide an adequate standard of loyalty for employer-administrators. This is because the proscriptive rules used by the Supreme Court do not provide adequate flexibility for determining the scope of the duty of loyalty in cases where there is an authorized conflict. In this Part, I also suggest an alternative standard, the *demonstrable partiality* standard, derived from cases dealing with other conflicted fiduciaries. In Part III, I discuss the ramifications of the choice between these standards for determining breach of duty. In Part IV, I turn to remedies and analyze the Court's reasoning on the availability of the constructive trust as a remedy for breach of fiduciary duty. I conclude that the Court was right to deny the constructive trust, but argue that the existing test should be revised to better account for the relationship between the wrong of disloyalty and the proprietary character of the remedy.

I. *Indalex*, in Brief

In 2009, Indalex Limited (*Indalex*), a Canadian subsidiary of Sun Indalex Finance, became insolvent as a result of the confluence of a variety of micro- and macro-economic factors. Following the insolvency, two groups of former Indalex employees sued Sun Indalex Finance, the trustee in bankruptcy of the United States Indalex debtors and Indalex's court-appointed Monitor. The suit centred on unpaid pension benefits under two employer-sponsored plans: one for salaried employees and another for executives. The plan for salaried employees was being wound up when insolvency proceedings were initiated; the plan for the executives had been closed but not wound up. The salaried employees' plan ended up having a wind up deficiency of approximately \$2 million as of December 31, 2008. The executives' plan had a funding deficiency of approximately \$3 million on a wind up basis as of January 1, 2008.

Indalex was the employer-administrator of both the salaried and executive plans, because it sponsored the plans and engaged in fiduciary

administration of the plans on the employees' behalf.¹⁷ Consequently, Indalex directors held two potentially conflicting fiduciary mandates. First, they enjoyed managerial authority over the company, to be exercised in the company's interests. Second, they enjoyed administrative authority over the pension plans, to be exercised in the interests of the plan members.

In late March 2009, Indalex's US parent filed for Chapter 11 bankruptcy protection. On April 3, 2009, Indalex, in turn, applied for and received a stay under the *Companies' Creditors Arrangement Act* (CCAA).¹⁸ The plan members did not receive notice of the application for this order. Insolvency proceedings were initiated with the goal of selling the US and Canadian companies as a going concern, and the companies pursued a common agreement for debtor-in-possession (DIP) financing. They successfully concluded a DIP financing agreement with a syndicate of banks. This agreement, authorized by court order on April 8, 2009, granted the DIP lenders super-priority over all other creditors to the extent of the borrowing limit (initially USD 24.4 million which was later increased to USD 29.5 million).¹⁹ The Court and the CCAA Monitor were of the view that DIP financing was necessary in the circumstances and in the best interests of Indalex. However, the members of the salaried and executive plans did not participate in, nor receive proper notice of, these proceedings.

On April 22, 2009, Morawetz J ordered an extension of the stay under the CCAA and approved plans for marketing the sale of Indalex's assets (the latter having been assigned a liquidation value of USD 44.7 million).²⁰ A court-sanctioned bidding process produced only one bid, in the amount of USD 30 million from SAPA Holding AB (SAPA). Under the terms of the bid, SAPA would not assume responsibility for the pension fund deficiencies. Despite opposition from plan members, on July 20, 2009 Campbell J approved the sale to SAPA and approved interim distribution of the sale proceeds to the DIP lenders.²¹ The plan members argued that

17. The fiduciary character of plan administration by employer-administrators was settled by the Supreme Court of Canada in *Burke v Hudson's Bay Co*, 2010 SCC 34, [2010] 2 SCR 273.

18. RSC 1985, c C-36.

19. See *Indalex* SCC, *supra* note 16 at paras 9, 11.

20. *Ibid* at para 13.

21. *Ibid* at para 15.

the sale proceeds were subject to a statutory deemed trust under section 57(4) of the *Pension Benefits Act (PBA)*²² and a constructive trust on the basis of breach of fiduciary duty by Indalex as plan administrator. By court order, the CCAA Monitor held USD 6.7 million of the sale proceeds in reserve pending judicial resolution of these claims.²³

On closing, Indalex owed USD 27 million to the DIP lenders, only USD 17 million of which was paid through distribution of the sale proceeds by the Monitor. Indalex US covered the USD 10 million shortfall in accordance with the terms of the DIP financing agreement and was thereby subrogated to the DIP lenders' super-priority.²⁴

Members of both plans brought motions on August 28, 2009, asserting that trusts in amounts equal to the pension shortfalls were enforceable against the proceeds retained by the CCAA Monitor. Indalex US resisted and asserted its claim to the proceeds on the basis of its status as highest ranking secured creditor. On February 18, 2010, these motions were dismissed by Campbell J, who found that the statutory deemed trust did not apply to either plan because the wind up deficiencies in the salaried plan were not *due* on the wind up date and the executive plan did not have wind up deficiencies.²⁵

An appeal by the plan members was unanimously allowed by the Ontario Court of Appeal.²⁶ Justice Gillese, writing for the Court, held that the statutory deemed trust did arise in respect of the salaried plan because it applied to all amounts due in respect of wind up deficiencies. She also held that, while the executive plan had not been wound up, members of both plans were entitled to a constructive trust over the sale proceeds based on several breaches of fiduciary duty by Indalex in its capacity as administrator of the plans.

The CCAA Monitor, Sun Indalex and Indalex US' trustee in bankruptcy appealed to the Supreme Court of Canada. The Supreme Court entertained four issues on the appeal: (1) whether the statutory deemed trust provided for by the *PBA* applies to wind up deficiencies; (2) assuming it does, whether it supersedes priority under the DIP agreement;

22. RSO 1990, c P.8 [*PBA*].

23. See *Indalex SCC*, *supra* note 16 at para 16.

24. *Ibid.*

25. *Indalex Ltd, Re*, 2010 ONSC 1114, 79 CCPB 301.

26. *Indalex Ltd, Re*, 2011 ONCA 265, 104 OR (3d) 641 [*Indalex CA*].

(3) whether Indalex had fiduciary duties to plan members when considering its options in respect of insolvency, and if so whether those duties were actionably breached; and (4) supposing Indalex had actionably violated its fiduciary duties to plan members, whether a constructive trust was an appropriate remedy. For present purposes, I will summarize only those portions of the reasons that relate to the third and fourth issues.

Before both the Ontario Court of Appeal and the Supreme Court of Canada, counsel for the plan members advanced their fiduciary disloyalty claims on the assumption that the proscriptive rules apply to employer-administrators. They argued that Indalex was liable to the extent that it was conflicted. According to the plan members, an actionable conflict arose from the moment that Indalex began to seriously consider CCAA proceedings. As such, these proceedings would inevitably threaten the interests of employees and disrupt the coordination of interests amongst stakeholders that is typically found in a solvent company. Insolvency usually means that some stakeholders will not get paid. The employees' interest in receiving promised compensation cannot easily be reconciled with the interests of other stakeholders which an employer must consider as a company approaches insolvency. Thus, the prospect of insolvency generates an actual conflict, which will be actionable if ignored.

Indalex argued that the roles it occupied should be differentiated. Indalex claimed that when it made decisions relating to the CCAA proceedings, it was operating in its role as *corporate employer*, not as *plan administrator*, and therefore could not be held liable to the plan members for disloyalty. In short, Indalex was not acting in a fiduciary capacity for plan members when the impugned decisions were made. Notwithstanding the existence of some precedent for this line of argument,²⁷ it was rightly rejected by both the Ontario Court of Appeal and the Supreme Court of Canada.²⁸ The argument is specious because it is impossible both in theory and in practice to segregate fiduciary mandates undertaken concurrently and executed in overlapping ways.

27. *Imperial Oil Ltd v Ontario (Superintendent of Pensions)*, 18 CCPB 198, 1995 CarswellOnt 2252 (WL Can) (Pension Commission).

28. Although, the Courts rejected it for different reasons. The Ontario Court of Appeal appears to have accepted that the analysis may be conducted in terms of roles but rejected the simplistic notion that a given decision may be made in only one capacity. The Supreme Court of Canada rejected the entire line of argument.

The Ontario Court of Appeal accepted the basic thrust of the plan members' argument. Justice Gillese, relying on the express language of section 22(4) of the *PBA*, held that:

Indalex was in a conflict of interest position. . . . The common law prohibition against conflict of interest is not confined to situations where the fiduciary's personal interest conflicts with those of the beneficiaries. It also precludes the fiduciary from placing itself in a position where it acts for two parties who are adverse in interest.²⁹

She found that on these facts, "the prohibition . . . governs the situation in which Indalex found itself in during the *CCAA* proceedings".³⁰ Given that the plan administration mandate was subordinated by Indalex to the corporate management mandate, Indalex was liable for disloyalty to the plan members. Justice Gillese imposed a constructive trust over the sale proceeds, but did so with little analysis of the bases on which constructive trusts may be awarded for breach of fiduciary duty.

The Supreme Court of Canada was divided on issues of wrong and remedy. A majority of the Supreme Court—represented in the judgments of Deschamps and Cromwell JJ—held that the proscriptive rules do not apply to employer-administrators. Both decisions emphasized that conflicts are inherent in the dual roles occupied by employer-administrators and held that, because these conflicts are implicitly authorized, the *mere existence* of a conflict cannot suffice to trigger liability.³¹ Instead, liability is a function of a conflicted fiduciary's failure to *respond properly* to conflicts. Justices Deschamps and Cromwell both concluded, for different reasons, that Indalex inadequately responded to a conflict and thus violated its fiduciary duty to the plan members. However, neither felt that a constructive trust was an appropriate remedy in the circumstances.

29. *Indalex CA*, *supra* note 26 at paras 140–41.

30. *Ibid* at para 142.

31. *Indalex SCC*, *supra* note 16. Justice Cromwell stated:

The existence of apparent conflicts that are inherent in the two roles being performed by the same party cannot be a breach of fiduciary duty because those conflicts are specifically authorized by the statute which permits one party to play both roles. . . . [T]he broader business interests of the employer corporation and the interests of pension beneficiaries in getting the promised benefits are almost always at least potentially in conflict.

Ibid at para 198.

Justice LeBel issued a strong dissent in which he objected to the apparently diminished standard of loyalty devised by the majority for employer-administrators: “[D]ual status does not entitle the employer to greater leniency in the determination and exercise of its fiduciary duties or excuse wrongful actions”.³² Justice LeBel held that the proscriptive rules were applicable and that there was a conflict “from the moment [Indalex] started to contemplate putting itself under the protection of the CCAA and propos[ed] an arrangement to its creditors”.³³ According to LeBel J, at that moment, Indalex ought to have recognized that an actual conflict had arisen and resigned in favour of an independent administrator. Having failed to do so, Indalex was liable for disloyalty. Justice LeBel also parted company with the majority on the question of remedy, concluding that there was “no error” in the decision of the Ontario Court of Appeal to award a constructive trust over the sale proceeds.³⁴

II. Divided or Multiple Loyalties?

Indalex is a good example of the difficulty in determining standards of conduct appropriate to conflicted fiduciaries. It shows how pervasive the proscriptive rules are and how deeply they have influenced our thinking about fiduciary law.³⁵ In order to identify alternative standards of conduct, we must ask fundamental questions concerning the nature of fiduciary loyalty more generally. Apart from, or beyond, avoidance of conflicts, what do we expect from fiduciaries when we expect them to be loyal? If fiduciary loyalty involves something beyond the avoidance of conflicts, does the presence of an authorized conflict—latent or actual—necessarily mean that a fiduciary’s loyalty is divided?

A. The Problem: Articulating Standards for Conflicted Fiduciaries

In *Indalex*, the Supreme Court of Canada clearly recognized that the occupation of conflicting mandates by a fiduciary complicates the interpretation and enforcement of the duty of loyalty. Ordinarily,

32. *Ibid* at para 266.

33. *Ibid* at para 269.

34. *Ibid* at para 277.

35. See Gold, “Loyalties”, *supra* note 9.

assumption of conflicting mandates is forbidden by the conflict of duty rule.³⁶ The conflict rules are notoriously strict.³⁷ In their typical formulation, they prohibit even the appearance of conflict: “[A] fiduciary who acts for two principals with *potentially* conflicting interests without the informed consent of both is in breach of the obligation of *undivided* loyalty Breach of the rule automatically constitutes a breach of fiduciary duty.”³⁸ The strictness of the conflict rules, and their suggestion of an *exclusive* or *indivisible* claim on the fiduciary’s discretion, is witnessed in the vast volume of ink spilled on fiduciary regulation of conflicting engagements of lawyers.³⁹ In the usual case, a fiduciary must avoid a conflict at all costs, or she must seek valid consent to the conflict from the beneficiaries. Without this consent, the fiduciary must validly tender her resignation from one of the mandates. In some cases, the fiduciary is successful in obtaining consent. In others, multiple conflicting mandates are authorized by statute. By what standard of loyalty is the conduct of fiduciaries to be measured when authorized conflicts exist?

36. See *Commonwealth Bank of Australia v Smith*, [1991] 42 FCR 390 (“[n]ot only must the fiduciary avoid . . . placing himself in a position of conflict between duty and personal interest, but he must eschew conflicting engagements” at 392). The Court cited this case approvingly in *Bristol & West Building Society v May, May & Merrimans*, [1996] 2 All ER 801 at 815–16 (Ch).

37. The strictness and breadth of the rules underlie the (probably untenable) general characterization of the duty of loyalty as functionally prophylactic. See e.g. *Harris v Digital Pulse Pty Ltd*, [2003] NSWCA 10. The court stated that fiduciary liability rules are “prophylactic in the sense that they tend to prevent the disease of temptation in the fiduciary—they preserve or protect the fiduciary from that disease. . . . The prevention of or protection from the relevant disease is assisted by the strictness of the standard imposed and the absence of defences justifying departures from it.” *Ibid* at paras 413–14.

38. *Mothew*, *supra* note 5 at 18–19 [emphasis added].

39. This is a matter that has been taken up in not less than three significant judgments of the Supreme Court of Canada in the last decade, not to mention numerous reports of bar associations and law societies and countless scholarly articles. See *R v Neil*, *supra* note 5; *Strother v 3464920 Canada Inc*, 2007 SCC 24, [2007] 2 SCR 177; *Canadian National Railway Co v McKercher LLP*, 2013 SCC 39, [2013] 2 SCR 649. See also CBA Task Force on Conflicts of Interest, *Conflicts of Interest: Final Report, Recommendations & Toolkit* (Ottawa: Canadian Bar Association, 2008); Federation of Law Societies of Canada, *Model Code of Professional Conduct* (Ottawa: FLSC, 2012), s 3.4–1; Devlin & Rees, *supra* note 15; Adam Dodek, “Conflicting Identities: The Battle over the Duty of Loyalty in Canada” (2011) 14:2 Leg Ethics 193.

In an important sense, an either/or approach to identifying standards of loyalty for conflicted fiduciaries is misguided. The authorization of a *conflict* does not mean tolerance of *conflicts* generally. Indeed, an authorization is ordinarily specific in respect of the kind(s) of conflicts that will be tolerated. For example, in *Indalex*, the conflict authorized was the latent one inherent in the occupation of plan administration and corporate management mandates. It was recognized and accepted that the corporate management mandate might conflict with the plan administration mandate. The fact that the proscriptive rules were held in abeyance in respect of *this conflict* did not mean that those rules were otherwise inapplicable. *Indalex's* directors could not, for instance, have escaped liability for personally appropriating funds payable to the plan on the basis that the conflict rules are inapplicable to their administration of the plan.

In a given case, more than one standard of conduct might determine a fiduciary's compliance with his duty of loyalty. The proscriptive rules may, and in most cases will, govern the discharge of a fiduciary mandate even where the fiduciary is conflicted. It is simply that the proscriptive rules govern decisions other than those that implicate the narrow category of *authorized* conflicts. It should be recognized that authorized conflicts will remain latent in the majority of decisions taken by a conflicted fiduciary. This suggests that, at least in the eyes of the law, a fiduciary can have multiple loyalties, and the mere possibility of a conflict between mandates does not imply that multiple loyalties are compromised or divided loyalties.

Accepting that the proscriptive rules will govern most decisions made by conflicted fiduciaries, the challenges associated with articulating an alternative standard of loyalty can be put more precisely. By what standard is the loyalty of a conflicted fiduciary to be measured when the fiduciary acts in the face of an authorized, latent conflict? How does that standard govern the conduct of the fiduciary when the latent conflict ripens? How does the alternative standard relate, in theory and in practice, to the proscriptive rules? If the suggestion that multiple loyalties can be robust loyalties is plausible, there ought to be answers to these questions.

B. *The Enduring Allure of the Proscriptive Rules*

The Supreme Court of Canada ultimately failed to convincingly address any of these questions in the *Indalex* decision, principally because they could not see beyond the proscriptive rules. Each of the justices analyzed the standard of conduct applicable to conflicted fiduciaries in terms of the proscriptive rules and *conflicts* instead of formulating a positive conception of fiduciary loyalty.

First, consider the reasons recognized by both Deschamps and Cromwell JJ: (a) employer-administrators face an authorized, latent conflict between their mandates as corporate managers and plan administrators; and (b) a latent conflict was actualized in the circumstances giving rise to *Indalex*. *Indalex* was thus one of the exceptional cases in which the proscriptive rules could not apply because the conflict was authorized. One might have thought this an ideal case in which to formulate an alternative standard of conduct. Instead, the Supreme Court chose to analyze *Indalex*'s conduct in terms of conflicts, maintaining their reliance on the proscriptive rules.

Justice Deschamps based her reasoning on section 22(4) of the *PBA*, which proscribes conflicts of interest (but not, it must be emphasized, conflicts of duty).⁴⁰ She held that the duty of loyalty requires employer-administrators to “ask . . . whether there is a potential conflict and, if so, what can be done to resolve the conflict”.⁴¹ The thought that conflicts can be resolved, and that once resolved, are innocent, seems plausible. However, quite apart from the obvious fact that the language of “managing”, “handling” or “resolving” conflicts is inconsistent with the strict, prophylactic character of the proscriptive rules, this approach is flawed. First, the suggestion that conflicts are innocent where resolved is unhelpful in respect of irresolvable conflicts. Many conflicts cannot be resolved without prejudice to the interests of one of the beneficiaries of the multiple mandates under which the fiduciary acts. In such cases, talk of resolution is polite cover for a decision which sacrifices the interests of one beneficiary for the sake of another. Second, the suggestion that an unavoidable conflict may be legitimately resolved implies that there are criteria which can be used to assess the propriety of actions taken to

40. *Supra* note 22, s 22(4).

41. *Indalex* SCC, *supra* note 16 at para 65.

effectuate resolution. It cannot be that *any* response to conflict will be adequate, in which case one must ask: “How can responses to conflicts be evaluated?” Justice Deschamps does not provide an answer.

Justice Cromwell offered a more detailed analysis. He found that the Ontario Court of Appeal “took much too expansive a view of the fiduciary duties owed by Indalex as plan administrator”.⁴² Justice Cromwell recognized that “as a general rule, a fiduciary has a duty of loyalty including the duty to *avoid* conflicts of interest”.⁴³ However, he rejected the Court of Appeal’s suggestion that the proscriptive rules were applicable, noting that in this case “the conflict itself was unavoidable”.⁴⁴

Curiously, given his rejection of the analytical framework associated with the conflict rules, Cromwell J used those rules to analyze the allegations of breach. Initially, he attempted to stipulate circumstances in which a conflict would be considered *real* or *serious* enough to trigger the application of a conflict rule. He concluded that “a situation of conflict of interest occurs when there is a *substantial risk* that the employer-administrator’s representation of the plan beneficiaries would be materially and adversely affected by the employer-administrator’s duties to the corporation”.⁴⁵ Here, Cromwell J borrowed language the Supreme Court had previously relied upon in adumbrating the conflict of duty rule as it applies to lawyers, this language in turn having been borrowed from the US *Restatement (Third) of the Law Governing Lawyers*.⁴⁶ Unfortunately, neither Cromwell J, nor the sources he relied upon, explain what makes a risk to the interests of a beneficiary “substantial”, or who is entitled to make this determination. In any event, the exercise was moot, as Cromwell J concluded his analysis by holding that the “simple existence” of a conflict is not wrongful. Like Deschamps J, Cromwell J held that liability should turn on the conflicted fiduciary’s response to a conflict. In his view, a conflicted fiduciary is actionably disloyal where

42. *Ibid* at para 182.

43. *Ibid* at para 186 [emphasis added].

44. *Ibid* at para 182.

45. *Ibid* at para 201 [emphasis added].

46. (2000) (“[a] conflict of interest is involved if there is a substantial risk that the lawyer’s representation of the client would be materially and adversely affected by the lawyer’s own interests or by the lawyer’s duties to another current client, a former client, or a third person” at §121). See also *R v Neil*, *supra* note 5.

she fails to respond properly to a conflict.⁴⁷ This conclusion raises the same problems as that of Deschamps J: By what criteria of propriety is a fiduciary's response to a conflict to be judged? Justice Cromwell does not provide an answer either.

In his dissent, LeBel J reasonably expressed concern with the majority's suggestion that conflicted fiduciaries are subject to a lesser standard of conduct, though he also failed to provide a practicable alternative. Justice LeBel argued that the proscriptive rules should have been applied. As I have indicated, these rules are applicable to many, perhaps most, decisions made by conflicted fiduciaries. However, a rule proscribing conflicts cannot be sensibly applied to a conflicted fiduciary in respect of decisions taken in respect of an authorized conflict.

C. Rethinking Fiduciary Loyalty: The Demonstrable Partiality Standard

Indalex leaves us with an unresolved puzzle. The case clearly shows that the content of the duty of loyalty is not exhausted by the proscriptive rules. The conflict rules supply default standards of conduct that govern the conduct of fiduciaries in most contexts. Nonetheless, in certain circumstances these rules cannot apply. Cases like *Indalex* might provide inspiration to those who have argued that the proscriptive rules reveal little about the positive character of fiduciary loyalty.⁴⁸ Clearly there must be something more to fiduciary loyalty than the avoidance of conflicts. Philosophical analyses of loyalty as a virtue or altruistic motivation may help one better understand the aspirational content of fiduciary loyalty, but more is needed to understand the content and effect of private law liability rules.⁴⁹ Fiduciary loyalty, being the object of an enforceable obligation, implies the existence of standards against which the conduct of a fiduciary can be measured. What standard of loyalty is appropriate to the conflicted fiduciary if it is not those supplied by the proscriptive rules?

The germ of a more profitable approach may be found in *Indalex*. In a very real sense, the proscriptive rules ensure that fiduciary relationships provide fertile ground for the cultivation of true loyalty by forbidding the

47. *Indalex* SCC, *supra* note 16 at paras 215–19.

48. L. Smith, "Motive, Not the Deed", *supra* note 9.

49. *Ibid.* See also Samet, "Fiduciary Loyalty", *supra* note 3.

fiduciary from placing herself in a position in which she may be tempted to be disloyal.⁵⁰ Despite this, as I have suggested elsewhere, standards of fiduciary loyalty cannot be fully understood without situating them in relation to the juridical nature of the fiduciary relationship.⁵¹ Here, then, is the insight that can be extracted from *Indalex*: The content of the duty of loyalty must be understood in light of the positive or performative character of a fiduciary mandate. One who undertakes a fiduciary mandate cannot live up to the fiduciary nature of the mandate merely by complying with proscriptions; the language of “mandate” itself is evocative of the expectation that fiduciaries *do something*. More specifically, it reflects the expectation that fiduciaries perform their mandate for, or on behalf of, their beneficiaries.

The performative character of fiduciary mandates is a reflection of the nature of fiduciary power, a topic which I address elsewhere.⁵² For present purposes, it suffices to say that the manner in which fiduciary mandates are performed will vary. In most cases, the fiduciary is expected to *act* in particular ways (e.g., to implement corporate policy, bring a lawsuit, administer a treatment, or make a buy or sell order). Ordinarily, the fiduciary will act under compulsion of the burden of performance on the basis of a discretionary *decision* that she has made (e.g., that a new procurement policy is in the best interests of the company or that market or firm-specific conditions support divestiture of an investment for an investor), although in some cases her decision may entail *inaction* (e.g., a decision that an investment should be held or that a policy that was reviewed should be unchanged). In any event, proper execution of a fiduciary mandate involves *performance* by the fiduciary. Performance of a fiduciary mandate occurs when a fiduciary decides whether to act on the particular powers associated with his mandate and if so, how to act.

The performative character of fiduciary mandates is not reflected clearly in the proscriptive rules themselves (though it is critical to understanding their purpose). It is, however, reflected fleetingly in the efforts of Deschamps and Cromwell JJ to articulate an alternative standard of loyalty for employer-administrators. Both justices, in emphasizing that

50. Irit Samet, “Guarding the Fiduciary’s Conscience: A Justification of a Stringent Profit-Stripping Rule” (2008) 28:4 Oxford J Leg Stud 763.

51. See Miller, “Justifying Fiduciary Duties”, *supra* note 5.

52. Paul B Miller, “The Fiduciary Relationship” in Gold & Miller, *supra* note 3, 63.

the actualization of latent conflicts calls for a *response*, recognized that the fiduciary's undertaking calls for positive acts of performance. While this is true of all fiduciaries, the conflicted fiduciary has a special burden of performance. Ordinarily, a fiduciary is not obligated to expressly justify the decisions he has taken as being in the best interests of his beneficiary, provided that he abides by the proscriptive rules. Instead, his decisions are treated with deference. Deference is supported by the grant of authority under which the fiduciary undertakes the powers associated with his mandate, but it is also supported by the fiduciary's abidance of the conflict rules. Absent a conflict, there is no reason a priori to doubt that the fiduciary will act other than in the interests of the beneficiary. The fiduciary is free (if not strictly obligated)⁵³ to make and to act on decisions that she subjectively believes are in the best interests of the beneficiary without worrying about being called to account for the reasons for which she acted. Things are different with conflicted fiduciaries where an authorized, latent conflict ripens. Here, I would argue, the fiduciary acts under an altered standard of conduct, one that requires him to be able to demonstrate that his decisions are justifiable in light of a more demanding conception of loyalty. I call this the *demonstrable partiality* standard of loyalty.⁵⁴

Under the *demonstrable partiality* standard, the fiduciary must be able to show that her decisions, and the actions pursuant to them, reflect clear partiality to the beneficiary (i.e., demonstrated commitment to advancing her interests or ends). Alternately, the fiduciary must resign from one of the mandates and take appropriate steps to ensure that the beneficiary's interests are protected by an authorized replacement.

Suppose that the fiduciary decides not to resign. She will carry on under both mandates notwithstanding the actualization of a latent conflict. Here, the fiduciary is on more precarious ground. But even in the face of actual conflict, multiple loyalties need not be divided ones. Actual conflicts can sometimes be avoided or resolved without injury to the interests of either beneficiary. Conflicting interests can be made

53. Compare L Smith, "Motive, Not the Deed", *supra* note 9.

54. I say *demonstrable* because the fiduciary must be able to demonstrate that she was loyal or faithful to the interests of the beneficiary under the standard. I refer to *partiality* because loyalty in this sense entails actual (and not merely pledged or promised) commitment to advancing the interests of a person or cause.

to coincide through prudent fiduciary administration. Alternative options may, for instance, be identified that are of mutual benefit to the beneficiaries of the multiple mandates, or that benefit one without injuring the interests of the other. This may be true of many decisions made by conflicted fiduciaries facing actual conflicts, but the law does not simply assume that conflicts will not result in compromised judgment. How, then, does a conflicted fiduciary demonstrate uncompromised loyalty under the *demonstrable partiality* standard?

In order to demonstrate uncompromised loyalty, the conflicted fiduciary must show that her decisions were reasonably calculated to advance or protect the interests of the beneficiary.⁵⁵ The *demonstrable partiality* standard calls upon the fiduciary to identify the reasons for which the decision was made (i.e., her basis for thinking that a decision would promote or secure the interests of the beneficiary) and to explain how those reasons influenced her course of conduct (i.e., to demonstrate the nexus between consideration of decision options and their projected impact on the beneficiary and subsequent decisions with respect to the exercise of fiduciary powers). The *demonstrable partiality* standard of loyalty places the fiduciary under significant decisional and procedural pressure. She must take special care in making and documenting her decisions in the expectation that she may be called upon to justify them. But these burdens provide necessary security for the expectation that

55. A *best-interests* standard is sometimes alluded to in the authorities, though it is usually not elaborated and enforced as such. See e.g. *Peoples Department Stores Inc (Trustee of) v Wise*, 2004 SCC 68, [2004] 3 SCR 461; *BCE Inc v 1976 Debentureholders*, 2008 SCC 69, [2008] 3 SCR 560. There are some similarities between the *best-interests* standard (if it may properly be called that) and the *demonstrable partiality* standard discussed here. Most notably, each suggests that fiduciary loyalty involves the fiduciary showing due regard for the interests of beneficiaries. However, the standards can be distinguished on two grounds. First, the *best-interests* standard is silent on whether due regard for the interests of beneficiaries is proven on a subjective or objective basis. By contrast, the *demonstrable partiality* standard indicates that it demands proof of compliance on an objective basis. Second, the *best-interests* standard is often referred to as though it is synonymous with the proscriptive rules, good faith requirements and other concepts loosely connected with the idea of fiduciary loyalty. This suggests that it may be better understood as a maxim that guides the formulation and implementation of standards. By contrast, as I explain below, the *demonstrable partiality* standard is derived from cases involving conflicted fiduciaries where it is clear that the proscriptive rules cannot apply. *Demonstrable partiality* is offered as an alternative standard of conduct and liability is judged accordingly.

conflicted fiduciaries will prove loyal to their beneficiaries by acting in their best interests.

The *demonstrable partiality* standard of loyalty has a respectable provenance, traced to cases in which courts were confronted with the problem of determining standards appropriate to conflicted fiduciaries. Cases involving conflicted lawyers and conflicted directors are especially prominent. Consider, for example, *Teck Corp Ltd v Millar*, in which the British Columbia Supreme Court scrutinized an incumbent board's response to a hostile takeover bid.⁵⁶ Incumbent directors facing a hostile bid must respond to the bid despite an actual conflict. As fiduciaries, they are obliged to act in the best interests of the corporation in responding to the bid. Yet, as individuals, the bid puts their position in the corporation at risk, which, in turn, engages their personal interests. What is an incumbent board to do? Resignation is not the solution, because any new director will face the same conflict once elected. The responsibility for the corporation will always remain with the board, but any decision made by them will be tinged by the suspicion that the personal interests of the members corrupted their judgment. By what standard of loyalty is the conduct of the board to be measured? Justice Berger in *Teck Corp* first framed the duty of loyalty in general terms: "The cases decided in the United Kingdom make it plain that directors, in the exercise of their powers, must act in what they bona fide consider to be the best interests of the company. . . . The cases decided in Canada proceed on the same footing."⁵⁷

Justice Berger then articulated the applicable standard, making it clear that a conflicted director must be able to show that his judgment was defensible on an objective basis:

I think the Courts should apply the general rule in this way: The directors must act in good faith. Then *there must be reasonable grounds for their belief*. If they say that they believe there will be substantial damage to the company's interests, then there must be reasonable grounds for that belief. If there are not, that will justify a finding that the directors were actuated by an improper purpose.⁵⁸

56. (1972), 33 DLR (3d) 288, [1973] 2 WWR 385 (BCSC) [cited to DLR].

57. *Ibid* at 309.

58. *Ibid* at 315–16 [emphasis added]. See also *First City Financial Corp Ltd v Genstar Corp* (1981), 33 OR (2d) 631, 125 DLR (3d) 303 (HCJ) ("[t]he right and indeed the obligation

The Court of Appeal in *Mothew* articulated the standard applicable to conflicted lawyers in similar terms, suggesting that all conflicted fiduciaries must be able to demonstrate substantial devotion to the interests of their beneficiaries, notwithstanding an authorized conflict. In the words of Lord Millett:

Even if a fiduciary is properly acting for two principals with potentially conflicting interests *he must act in good faith in the interests of each* and must not act with the intention of furthering the interests of one principal to the prejudice of those of the other . . . *He must serve each as faithfully and loyally as if he were his only principal.*⁵⁹

Lord Millett's way of putting the standard makes it clear that, in the eyes of the law, multiple fiduciary loyalties need not be divided ones. The *demonstrable partiality* standard sets terms which, if abided, ensure that multiple loyalties will remain robust in the face of conflicting interests.

In contrast to *demonstrable partiality*, the proscriptive rules collectively express an *exclusive-interest* standard of fiduciary loyalty. Whatever the fiduciary does, she must act in the sole interest of the beneficiary. The mere possibility of a conflict will result in liability. The proscriptive rules are appropriate default standards of loyalty, but as we have seen, there are circumstances in which they are unworkable. One such set

of directors to take steps that they honestly and *reasonably* believe are in the interests of the company and its shareholders in a take-over contest or in respect of a take-over bid, is perfectly clear and unchallenged" at 646 [emphasis added]; *Re Olympia & York Enterprises Ltd and Hiram Walker Resources Ltd* (1986), [1987] 59 OR (2d) 254, 37 DLR (4th) 193 (HCJ) [cited to OR] ("[i]t matters not when the directors act in the best interests of the company and in good faith that they also benefit as a result" at 271); *347883 Alberta Ltd v Producers Pipelines Inc*, [1991] 80 DLR (4th) 359, 4 WWR 577 (Sask CA) [cited to DLR].

[W]hen a corporation is faced with susceptibility to a take-over bid or an actual take-over bid, the directors must exercise their powers in accordance with their overriding duty to act *bona fide* and in the best interests of the corporation even though they may find themselves, through no fault of their own, in a conflict of interest situation. If, after investigation, they determine that action is necessary to advance the best interests of the company, they may act, but the *onus will be on them to show that their acts were reasonable* in relation to the threat posed and were directed to the benefit of the corporation and its shareholders as a whole.

Ibid at 402 [emphasis added].

59. *Mothew*, *supra* note 5 at 19 [emphasis added].

of circumstances is that in which a fiduciary acts under an authorized conflict. Conflicted fiduciaries are governed by the proscriptive rules, except in the face of an authorized conflict, when a different standard applies. The *exclusive-interest* standard then gives way to a more demanding *demonstrable partiality* standard, whereby the fiduciary must act in a manner reasonably calculated to protect or advance the interests of the beneficiary.

III. Standards in Action: Guiding and Evaluating Conduct

A. *The Functions of Standards of Conduct*

A standard of conduct, if it is sufficiently clear, promotes respect for private law duties in at least two ways. First, it dictates conditions of compliance for those who are subject to a legal duty.⁶⁰ Second, insofar as conditions of compliance ground liability, a standard of conduct enables consistent and predictable adjudication and enforcement of private law duties. In announcing clearly and authoritatively what duties require, standards of conduct promote the law's aim of fostering social order in a manner consistent with rule of law values.⁶¹

A standard of conduct that is unclear for any reason (e.g., by virtue of vagueness, unnecessary ambiguity, incompleteness or incoherence) will be deficient in its capacity to secure respect for private law duties. An unclear standard does not function well as a norm because those whose conduct or deliberations are to be guided by it can never be confident in their knowledge of what it requires.

B. *The Dysfunctionality of the Indalex Standard*

As I have explained above, the standards posited by the majority of the Supreme Court of Canada in *Indalex* are unclear. The proscriptive rules are effective as liability rules because they clearly and unambiguously

60. See Stephen A Smith, "The Normativity of Private Law" (2011) 31:2 Oxford J Leg Stud 215.

61. See Lon L Fuller, *The Morality of Law* (New Haven: Yale University Press, 1964).

prohibit fiduciaries from being in a position of conflict.⁶² That kind of prohibition is obviously unworkable for fiduciaries acting under an authorized conflict, but the alternative proposed by Deschamps and Cromwell JJ can hardly be considered a standard of conduct at all. Both justices say that conflicted fiduciaries are obliged to respond appropriately to the ripening of an authorized conflict, but criteria of propriety are not provided. Absent such criteria, it is impossible to say, on the basis of the standard itself, whether a given response to a conflict is appropriate.

Problems with the *appropriate response* standard are evident in *Indalex*. These problems can be found in the Supreme Court's decision, not in the ultimate determination of whether or not there was breach, but in the explanation of the basis for that finding. The facts of the case made it easy for the judges to work with an underspecified standard. After all, *Indalex* did nothing in response to the conflict it faced. On any reasonable understanding of a standard requiring an appropriate response to a situation or event, manifest indifference is not an appropriate response. Nevertheless, Cromwell and Deschamps JJ came to different conclusions on the timing of breach (i.e., when *Indalex* ought to have responded to the conflict) and the wrongful character of the conduct that constituted breach (i.e., how *Indalex* ought to have responded to the conflict).

Justice Deschamps acknowledged that there was an actual conflict from the moment that it became clear that *Indalex* was facing insolvency, given that the prospect of insolvency entailed risk to the interests of the plan beneficiaries. *Indalex*, as plan administrator, would be called upon to claim accrued contributions from itself as an enterprise and employer, notwithstanding that insolvency entails fracturing of interests amongst stakeholders. According to Deschamps J, at that moment, *Indalex* was obliged to do something: “[A]s soon as it saw, or ought to have seen, a

62. The proscriptive rules have been criticized on many grounds but not on the basis of lack of clarity. Indeed, some think that they overreach, and over-deter, for the sake of the clarity afforded by categorical or “bright line” prohibitions. Economists, especially, tend to view the proscriptive rules this way. See generally Robert Cooter & Bradley J Freedman, “The Fiduciary Relationship: Its Economic Character and Legal Consequences” (1991) 66:4 NYUL Rev 1045. *Contra* Lionel D Smith, “Deterrence, Prophylaxis and Punishment in Fiduciary Obligations” (2013) 7 J Equity 87 [L Smith, “Deterrence, Prophylaxis and Punishment”].

potential for conflict, Indalex should have taken steps to ensure that the interests of the Plan Members were protected”.⁶³

However, Deschamps J refused to find that Indalex’s decision to commence insolvency proceedings entailed a breach by Indalex. This is puzzling given that she had admitted that this decision necessarily imperilled the interests of plan members. Justice Deschamps’ reasoning is incongruous; she acknowledged the risk to the interests of plan beneficiaries generated by a conflict, suggested that conflicted fiduciaries are duty-bound to respond to such risks, and yet said that a fiduciary may take steps which heighten a risk associated with a conflict. She eventually concluded that Indalex was only in breach when it filed for court approval of the DIP financing arrangements. By this stage, the risk to the interests of plan beneficiaries was fully ripe, and most troublingly, Indalex, as the fiduciary, was instrumental in the conflict’s maturation.

Concluding that the breach occurred when Indalex decided to pursue DIP financing, Deschamps J reasoned that Indalex ought to have responded to the conflict by “at least giv[ing the beneficiaries] the opportunity to present their arguments”.⁶⁴ The employees could have been provided such an opportunity through notice of the DIP financing motion.

Justice Deschamps’ conclusion about the proper response to this conflict seems inconsistent with some basic presuppositions of fiduciary law. Accepting that fiduciaries wield fiduciary powers in order to further the interests of their beneficiaries, it is curious to suggest that a conflicted fiduciary may prove loyal to her beneficiary not by exercising judgment for her benefit, but merely by giving the beneficiary a chance to fend for herself. The suggestion is all the more curious where the beneficiary is to fend for himself in a conflict which the fiduciary has caused and in which the fiduciary has taken an adverse position.

Justice Cromwell draws similar conclusions for reasons that are different but equally puzzling. His analysis is largely framed in terms of identifying the *presence* of a conflict rather than assessing *responses* to conflicts. He begins his analysis by redefining conflict of interest, where he holds that to be real or actionable, a conflict must present a “substantial risk that [the administration of the fiduciary mandate] would

63. *Indalex SCC*, *supra* note 16 at para 68.

64. *Ibid* at para 73.

be materially and adversely affected”.⁶⁵ This redefinition of conflicts led him to the otherwise inexplicable conclusion that Indalex’s decision to initiate insolvency proceedings “did not, on its own, give rise to any conflict of interest or duty”.⁶⁶

In supporting this conclusion, Cromwell J continued to subtly but significantly shift the ground upon which conventional conflicts analysis rests. Justice Cromwell held that there was no conflict when the insolvency proceedings were initiated because Indalex’s employees could not have hoped for better if Indalex had acted otherwise. The nexus between the existence of a conflict and likely outcomes for beneficiaries is spurious. The issue of outcomes goes to whether a fiduciary’s decisions (including one taken in response to a conflict) may be deemed favourable in all the circumstances (i.e., whether it serves, to the extent possible, the interests of beneficiaries). Outcomes have no bearing on the existence of a conflict (i.e., whether the interests of beneficiaries were imperilled by virtue of a situation generating adversity of interest).

Justice Cromwell also made the strange counterfactual argument that Indalex was not obliged to respond to a conflict by providing notice to the plan members because if it were simply their employer, it “would not have been under an obligation to tell the administrator that it was planning to enter CCAA proceedings”.⁶⁷ The reasoning here is obviously specious. One cannot argue that there is no breach of fiduciary duty on the basis that, were one not a fiduciary, one would not be subject to the duty in question. It is well known that fiduciaries are subject to a duty of candor, requiring disclosure of information

65. *Ibid* at para 201. Justice Cromwell does not distinguish between actual and possible conflicts, nor does he address the former in terms of the realization of latent conflicts. Instead, he seems to think that the existence of a conflict is a function of the magnitude and probability of a risk associated with it. This is implausible. Magnitude and probability are measures of the degree of risk of an adverse outcome, not ways of determining the presence of a conflict (i.e., a situation in which the adversity of interests of two or more people entails risk of prejudice to the interests of at least one of them). *Ibid*. See also the definition I establish of conflict, *supra* note 10.

66. *Indalex SCC*, *supra* note 16 at para 204.

67. *Ibid* at para 210.

material to the interests of their beneficiaries.⁶⁸ Failure to give notice is not merely evidence of disloyalty; it is an independent actionable wrong.

Justice Cromwell next considered the implications of Indalex's decision to seek DIP financing. Here, he acknowledged that there was a conflict insofar as the "DIP orders could easily have the effect of making it impossible for Indalex to satisfy its funding obligations to the plan beneficiaries".⁶⁹ He found a breach in "Indalex's failure to take steps so that the plan beneficiaries would have the opportunity to have their interests protected in the CCAA proceedings".⁷⁰ Notice the language. Justice Cromwell does not suggest that Indalex ought to have protected the interests of the beneficiaries, nor does he suggest that they may rightly have been left to fend for themselves. He instead suggests that Indalex ought to have done something to ensure that *someone* looked out for the interests of the beneficiaries. What could Indalex have done?

In the eyes of Cromwell J, Indalex should have brought the conflict to the attention of the CCAA judge and left the decision to him. It is difficult to see how this reflects the application of anything like a fiduciary standard of conduct. Courts do often exercise extraordinary powers of judicial review in supervising fiduciaries. While the Courts have authority to exercise these powers, it is ordinarily only at the insistence of the beneficiary where the fiduciary is alleged to have acted wrongfully or in excess of authority. Barring this, a fiduciary is presumed personally responsible for ministering to the interests of his beneficiary. Judges are not substitute fiduciaries and are especially ill-suited to this role when they have adjudicative responsibilities which require them to strike a fair balance between the competing interests of various parties.

C. Implementing the Demonstrable Partiality Standard

The flaws in the reasoning of Deschamps and Cromwell JJ concerning the timing and nature of breach reflect deficiencies in the standard of conduct with which they were working. Again, the *appropriate response* standard is not a proper standard of conduct because it does not provide

68. See generally Richard RW Brooks, "Knowledge in Fiduciary Relations" in Gold & Miller, *supra* note 3, 225.

69. *Indalex SCC*, *supra* note 16 at para 214.

70. *Ibid* at para 215.

any criteria for action or judgment. A standard without normative content (i.e., without action- and/or reason-guiding rules) risks being interpreted and enforced in a way that is conceptually and normatively dissonant with the underlying duty. This risk was realized in *Indalex*.

The Court might have fared better had it worked with a clearer standard of conduct, such as the *demonstrable partiality* standard. This standard promotes responsible handling of conflicts by placing conflicted fiduciaries under the burden of proving that decisions taken in the face of an actual conflict were reasonably calculated to serve the interests of their beneficiaries. Conditions of compliance may be readily derived from this standard. To my knowledge, these conditions have not been exhaustively articulated in the authorities. However, I suggest that the following conditions are implicit in the standard itself:

- First, in general, the conflicted fiduciary must take extra care in her decision-making, recognizing that it will be subject to heightened scrutiny;
- Second, the conflicted fiduciary must identify the way(s) in which the beneficiary's interests are engaged by particular matters for decision;
- Third, the conflicted fiduciary must evaluate the nature and extent of actual conflict between the interests of beneficiaries of the multiple mandates under which she acts;
- Fourth, the conflicted fiduciary must identify decision options and project their likely impact on pertinent interests of the beneficiaries;
- Fifth, the conflicted fiduciary must take note of facts, evidence or opinions (including any independent advice) supporting these projections and should document this information;
- Sixth, based on the documented information, the conflicted fiduciary must decide whether the conflict can be resolved without prejudice to the interests of either beneficiary; and
- Seventh, if the conflicted fiduciary concludes that the conflict cannot be so resolved, she must offer her resignation from one of the mandates and, if accepted, ensure continuity of competent fiduciary administration of the mandate. Alternatively, if the conflicted fiduciary instead believes that there are options that will prejudice

neither beneficiary, she must choose the option that she reasonably believes will best serve the interests of both.

Indalex obviously failed to meet this standard. It did nothing to protect the interests of plan members. On the contrary, it acted to the obvious prejudice of their interests. However, reflection on Indalex's failings is less instructive than consideration of what the *demonstrable partiality* standard suggests ought to have been done. Employer-administrators act under a latent conflict of duty. Where ripened, the conflict triggers the *demonstrable partiality* standard. The standard provides clear guidance enabling a more fine-grained analysis of Indalex's conduct than was possible under the *appropriate response* standard. Indalex, as a conflicted fiduciary, ought to have taken extra care in its decision making. Extra care could be shown by specific advertence to, and open deliberation about, contending demands it was facing. Without a doubt, insolvency quickly ripens the conflict facing employer-administrators. The company's core interests lie in survival and showing appropriate respect for the economic interests and legal rights of all of its stakeholders. The employees' core aims are continued employment (if possible) and being paid what they are owed. When it realized that insolvency was nearly certain, Indalex ought to have considered what CCAA proceedings might mean for plan members and, more specifically, whether, and to what extent, the options before it entailed irresolvable conflict between the interests of the company and the plan members. It may well have been, and likely was, the case that the viable options before Indalex were few and that none would permit it to simultaneously pursue the best interests of the company and the plan members. If that was the case, Indalex ought to have: (1) documented the viable options open to it, the basis for pursuing these options and not others, and the implications of the options for plan members; and (2) resigned from its plan administration mandate on the basis of anticipated prejudice to the interests of plan members.

Lest it be thought that resignation offers conflicted fiduciaries an easy out, it should be borne in mind that the *demonstrable partiality* standard governs exit from, as well as execution of, a fiduciary mandate. Compliance with the standard requires that the fiduciary facilitate the continuity of competent fiduciary administration by giving due notice of her intent to resign, identifying a suitable independent administrator,

and ensuring that the replacement administrator has access to, and is apprised of, all information material to execution of the mandate. Due notice implies that sufficient time has been allocated for the orderly transfer of the mandate. Resignation should not be considered effective in insulating a fiduciary from liability if the timing is such that the interests of a beneficiary were prejudiced. Therefore, a conflicted fiduciary ought to prepare for resignation as soon as she believes that she may have to pursue an option adverse to the interests of her beneficiary. In this case, Indalex ought to have given notice of its intent to resign and made necessary preparations from the moment it identified DIP financing as the only viable option facing the company. The requirement of timely resignation ensures that the interests of beneficiaries receive considered attention before anticipated harm becomes more or less certain.⁷¹

This brief illustration of the *demonstrable partiality* standard shows that while it is rather onerous, it ensures that the multiple loyalties of a fiduciary are not diminished by the presence of a conflict. The standard fosters fidelity in the face of conflict and it supports principled resignation where a conflict makes the administration of multiple mandates untenable.

IV. Remediating Fiduciary Disloyalty

Ordinarily, the commission of a civil wrong means that the individual who suffered it will be entitled to a court-ordered remedy from the individual who perpetrated it. Remedies provide security for primary rights and duties by underscoring the continuing normativity of the reasons underlying them and by ensuring that material gains and losses lie where they should.⁷² Remedies are critically important to private

71. Justice Cromwell reasoned that the fact that plan members' interests were not represented at the initial CCAA proceedings was legally inconsequential because it was unlikely to have had an impact on the outcome of those proceedings. However, the fact that outcomes are more or less certain is beside the point, for the essential character of a fiduciary mandate is one of *representation*. A fiduciary ensures that the beneficiary's interests are represented and pursued to the extent possible through that representation. The fiduciary is not a guarantor. Conversely, the fact that she cannot influence, much less secure, an outcome is no excuse for a failure of representation.

72. See generally John Gardner, "What is Tort Law For?: Part 1—The Place of Corrective Justice" (2011) 30:1 Law & Phil 1. See also Miller, "Justifying Fiduciary Remedies", *supra* note 9 at 580–82.

law because they are the principal means by which civil wrongdoers are made personally accountable to their victims. However, as others have observed, corrective justice is served not by courts acting on their own prerogative but by individual litigants (plaintiffs) exercising powers to demand accountability through civil actions.⁷³ Corrective justice must be actively sought, and it is not imposed on those who acquiesce in, are indifferent to, or wish to forgive civil wrongdoing.

An unnoticed corollary of this is that there are important limits on seeking accountability on terms of corrective justice through civil action. The powers of litigants to pursue recourse are conditional on properly pleaded causes of action (i.e., specified allegations of wrongdoing) and claims for relief (i.e., petitions for remedial or injunctive orders). A litigant who improperly pleads a cause of action (e.g., by neglecting to allege a wrong that was committed) or claim for relief (e.g., by requesting a remedy that is not available) may have a wrong suffered go un-remedied. The plaintiff's *responsibility* to properly pursue civil actions arguably reveals the contingent character of corrective justice more vividly than their *powers* to initiate civil actions.

A. The Constructive Trust as a Fiduciary Remedy

The contingent character of corrective justice is illustrated in discussions of remedies in *Indalex*. While the Ontario Court of Appeal and Supreme Court of Canada were unanimously of the view that *Indalex* was in breach of its fiduciary duty, there was disagreement over the availability of the remedy claimed by the plan members. The Ontario Court of Appeal and LeBel J, in dissent at the Supreme Court, held that a constructive trust was an appropriate remedy, while the majority of the Supreme Court held otherwise. As a result, the wrong suffered by the plan members went un-remedied on the basis that they claimed a remedy to which they were not entitled. I believe the majority was right to conclude that conditions requisite to awarding a constructive trust for breach of fiduciary duty were not met in *Indalex*. However, because of certain ambiguities in the

73. See John CP Goldberg & Benjamin C Zipursky, "Torts as Wrongs" (2010) 88:5 Tex L Rev 917; Jason M Solomon, "Equal Accountability Through Tort Law" (2009) 103:4 Nw UL Rev 1765; Andrew S Gold, "A Theory of Redressive Justice" (2014) 64:2 UTLJ 159.

law, the Supreme Court misstated these conditions and thus the basis for refusing the remedy.

The justices agreed on the law but disagreed on its application. The law governing the availability of the constructive trust as a remedy for breach of fiduciary duty is outlined in *Lac Minerals Ltd v International Corona Resources Ltd*⁷⁴ and *Soulos v Korkontzilas*.⁷⁵ In *Lac Minerals*, the Supreme Court emphasized that a constructive trust is an exceptional remedy, which “should only be awarded if there is reason to grant to the plaintiff the additional rights that flow from recognition of a right of property”.⁷⁶ Unfortunately, the Court did not address the critical question: What kind of reasons justify awarding a proprietary remedy like the constructive trust? In *Soulos*, the Supreme Court provided a more comprehensive set of conditions for awarding the remedy and was slightly more suggestive about the kinds of reasons that justify it. The *Soulos* test provides that:

First, the defendant must have been under an equitable obligation, that is, an obligation of the type that courts of equity have enforced, in relation to the activities giving rise to the assets in his hands;

Second, the assets in the hands of the defendant must be shown to have resulted from deemed or actual agency activities of the defendant in breach of his equitable obligation to the plaintiff;

Third, the plaintiff must show a legitimate reason for seeking a proprietary remedy, either personal or related to the need to ensure that others like the defendant remain faithful to their duties and;

Fourth, there must be no factors which would render imposition of a constructive trust unjust in all the circumstances of the case (e.g., the interests of intervening creditors must be protected).⁷⁷

Awarding a constructive trust as a discretionary remedy for equitable wrongs is always controversial in an insolvency context because it disrupts the default ranking of creditor priorities.⁷⁸ This issue finds explicit recognition in the fourth condition, where the availability of the remedy is

74. [1989] 2 SCR 574, 61 DLR (4th) 14 [*Lac Mineral* cited to SCR].

75. [1997] 2 SCR 217, 146 DLR (4th) 214 [*Soulos* cited to SCR].

76. *Supra* note 74 at 678.

77. *Supra* note 75 at 241.

78. See Emily L Sherwin, “Constructive Trusts in Bankruptcy” [1989] 2 U Ill L Rev 297;

made defeasible by “unjust factors”, which go unidentified save in respect of creditors’ interests. Given the general concern over constructive trusts defeating the reasonable expectations of creditors, and given that this concern was a focal point of arguments made before the Supreme Court, it is surprising that the Supreme Court did not focus on it. One can only speculate that Deschamps and Cromwell JJ might have been influenced by the forceful—and frankly compelling—argument that *Indalex* was not an ordinary case for protection of creditor interests because those interests were being asserted by Indalex US (via subrogation) against the employees of its own subsidiary. Indalex US was hardly an innocent third party creditor.⁷⁹

The majority of the Supreme Court thus advisedly focused on the core requirement associated with the other conditions in *Soulos*, namely, that the plaintiff must establish a proper nexus between the wrong suffered and the remedy claimed.⁸⁰ The first three *Soulos* conditions elaborate upon elements of this requirement, however vaguely. It is not entirely clear what is meant by “agency activities”,⁸¹ nor is it clear how a plaintiff is to establish a “personal”, “legitimate reason” for making a claim for proprietary rather than personal relief. Taking it on its face, the test seems to say, at least in respect of fiduciary wrongs, that a disappointed beneficiary must be able to show that the breach involved appropriation of an asset that was subject to the particular mandate on which the fiduciary relationship and attendant duties were founded. As the test is unclear, I hazard the following restatement, which I hope may be seen as extending and sharpening the *Soulos* test as it relates to fiduciaries without doing violence to it:

Andrew Kull, “Restitution in Bankruptcy: Reclamation and Constructive Trust” (1998) 72:3 Am Bank LJ 265.

79. See *Indalex CA*, *supra* note 26. Justice Gillese stated, “[t]o permit Sun Indalex to recover on behalf of Indalex U.S. would be to effectively permit the party who breached its fiduciary obligations to take the benefit of those breaches, to the detriment of those to whom the fiduciary obligations were owed.” *Ibid* at para 199.

80. Donovan WM Waters, Mark R Gillen & Lionel D Smith, eds, *Waters’ Law of Trusts in Canada*, 4th ed (Toronto: Carswell, 2012) at 494. Making out a nexus between the wrong and the remedy is critical because “trust rights are held in specific assets, and are not granted generally or over whichever assets a plaintiff chooses”. *Ibid*.

81. Of course, many fiduciaries are not agents. Trustees are not agents of settlors or beneficiaries, nor are directors agents of corporations. Their activities involve exercise of other-regarding powers but they cannot for that reason be considered agency activities.

A beneficiary will have made out an appropriate connection between the wrong of disloyalty and the remedy of constructive trust when:

- (a) the asset claimed via constructive trust falls within the specific mandate under which the fiduciary acted for the beneficiary (i.e., the asset must have been made subject to, or have arisen from, the exercise of discretionary powers vested in the fiduciary under her mandate to act for the beneficiary);⁸²
- (b) the fiduciary breached her duty of loyalty directly in relation to her handling of the asset;⁸³ and
- (c) the beneficiary has, by virtue of existing rights relative to the asset or the powers exercised in relation to it, a personal basis for claiming the asset rather than its monetary equivalent.⁸⁴

B. Linking Wrong and Remedy

The majority of the Supreme Court of Canada rightly concluded that the plan members did not have a viable claim to a constructive trust because they could not establish the requisite connection between Indalex's disloyalty and the proceeds of sale of the company. However,

82. This condition sharpens the first and second conditions in *Soulos*, making it clear that the wrong and remedy are inextricably bound up with the legal form of the fiduciary relationship and the location of the assets claimed within the ambit of that relationship (whether the location is a function of the fact that the assets were made subject to fiduciary powers when the relationship was initiated or carried out, or by virtue of the fact that the fiduciary was mandated to acquire the assets for the beneficiary).

83. This condition clarifies that the wrong must implicate the handling of the asset (as contrasted with wrongs that have no direct bearing on the fiduciary's handling of an asset within the ambit of the fiduciary relationship, such as violation of the conflict of interest rule through pursuit of a non-pecuniary personal interest).

84. This condition stipulates the "personal", "legitimate" reasons that a beneficiary could have for claiming an asset via constructive trust. They are reasons derivable from pre-existing property rights enjoyed in relation to the asset or rights in relation to the exercise of fiduciary power relative to the asset (powers which may extend to the acquisition, possession, use, and/or alienation of the asset). These rights are derivable from the form of the fiduciary relationship and their implications for disposition of the asset depend on the nature of the powers enjoyed by the fiduciary (i.e., what capacities the fiduciary has to manage, acquire or dispose of the asset).

neither Deschamp nor Cromwell JJ explained the nature of the required connection well.

Justice Deschamps' reasons on this point are exceedingly brief. She said, "it is settled law that proprietary remedies are generally awarded only with respect to property that is directly related to a wrong or that can be traced to such property. . . . [T]his condition was not met in the case at bar".⁸⁵ She did not explain how an asset claimed under constructive trust may be proved to be "directly related" to a wrong. There are many ways an asset can be related to a wrong, but to say that the relationship must be direct rather than indirect does not assist greatly in determining whether a beneficiary should be claiming a personal rather than a proprietary remedy. It is simply unclear in Deschamps J's judgment precisely *why* the plan members failed to establish their claim to a constructive trust.

Justice Cromwell's reasons are clearer in this respect. He found that the Ontario Court of Appeal "erred in principle in finding that the asset in this case *resulted from* the breach of fiduciary duty".⁸⁶ His reasons suggest that the requisite connection between wrong and remedy is one of cause-and-effect. An asset can be claimed via constructive trust only if one can show that the wrong in some sense produced the asset. Justice Cromwell continued:

[A] remedial constructive trust for a breach of fiduciary duty is only appropriate if the wrongdoer's acts *give rise* to an identifiable asset . . . In my view, Indalex's failure to meaningfully address conflicts of interest that arose during the CCAA proceedings did not *result in* any such asset.⁸⁷

To underscore the point, he further stated that "it must be shown that the breach *resulted in* the assets being in Indalex's hands, not simply, as the Court of Appeal thought, that there was a 'connection' between the assets and 'the process' in which Indalex breached its fiduciary duty".⁸⁸

This view of the required connection between wrong and remedy is both too broad and too narrow. It is too broad because it suggests that a constructive trust may arise wherever a fiduciary realizes a gain from disloyalty. This is problematic because it implies that this may occur even

85. *Indalex* SCC, *supra* note 16 at para 78.

86. *Ibid* at para 224 [emphasis added].

87. *Ibid* at para 227 [emphasis added].

88. *Ibid* at para 230 [emphasis in original].

if the beneficiary did not have an existing legal interest in the asset under the mandate. It goes so far as to suggest that a constructive trust may arise even where the asset does not fall within the mandate under which the fiduciary acted. It is too narrow in that it suggests that a constructive trust will only arise if the wrongful conduct of the fiduciary *itself* results in the asset claimed. This excludes the core situation in which awarding constructive trusts is common and uncontroversial. These cases involve the appropriation of an asset owned (in a legal or equitable sense) by the beneficiary (e.g., misappropriation of trust property by a trustee, or diversion of corporate revenue by a director). Breach in these cases *produces* nothing, but instead involves a kind of conversion or wrongful taking.

Justice Cromwell's analysis reflects ambiguities in the *Soulos* test. In *Soulos*, it was said that "assets in the hands of the defendant must be shown to have resulted from deemed or actual agency activities of the defendant".⁸⁹ Following Cromwell J, this might be taken to mean that the assets must have been produced through the wrongful conduct of the fiduciary. Yet, an alternative interpretation would enable better conformity between the test and the authorities from which it was derived. To establish the requisite connection between wrong and remedy, a beneficiary must establish one of two things: (1) a pre-existing legal or equitable interest in the asset; or (2) that the asset was generated by, or placed in the possession of, the fiduciary through the exercise of fiduciary powers.⁹⁰ In both circumstances, the fiduciary's present possession of the asset is contingent on her receipt and/or execution of a fiduciary mandate. In the former situation, the fiduciary has privileged access to an existing asset by virtue of her fiduciary mandate, and the very same mandate requires her to maintain and/or manage it in the interests of the beneficiary. In the latter situation, the fiduciary has the privileged ability to generate or attract an asset for the beneficiary by virtue of her mandate and the powers associated with it.

Supposing that this account is accurate, we can now better appreciate the flaw in the plan members' claim for a constructive trust. The remedy

89. *Supra* note 75 at 241.

90. The claim must be exclusively held by an individual beneficiary asserting her personal right or that of a class of beneficiaries who collectively are exclusively entitled to the fiduciary's loyalty under the mandate in question. A beneficiary whose right is not exclusive cannot, in justice, be granted more by way of remedy than she is entitled to by right.

was inappropriate because the asset claimed lay entirely beyond the plan administration mandate. The plan members, via the plan, had no pre-existing legal or equitable interest in the proceeds or the assets sold to generate the proceeds. The assets were corporate property. The plan members had a contractual right to promised payments, but that right was not secured by a charge against the assets of the company. The fact that this right could be asserted *against* company assets in insolvency does not imply an existing proprietary interest *in* the assets. Nor could the plan members show that the assets were either generated or received by Indalex under its mandate to administer the plans. The assets were generated in and through the insolvency proceedings and were directly traceable to corporate property—insofar as they were proceeds of the sale of the same. Handling of the assets was within the purview of the fiduciary mandate of Indalex directors to manage the company. How these assets were handled bore upon, but did not fall within, the distinct fiduciary mandate under which Indalex administered the plans.

Conclusion

Fiduciary relationships in which the fiduciary is authorized to be in a position of conflict raise several jurisprudential questions. Can a conflicted fiduciary be loyal in any meaningful sense? If so, how can the loyalties of a conflicted fiduciary be demonstrated? In this article, I have addressed these questions in light of the Supreme Court of Canada's decision in *Indalex*. There, the majority of the Supreme Court recognized that the loyalty of conflicted fiduciaries cannot be measured by the conventional proscriptive rules, but it failed to offer a reasonable alternative. This is unfortunate because an alternative standard of loyalty—the *demonstrable partiality* standard—can be derived from other cases involving conflicted fiduciaries. Application of this standard may have helped the Supreme Court reach consistent conclusions on the timing and nature of breach. Most importantly, it would have enabled the Supreme Court to avoid making the dangerous suggestion that conflicted fiduciaries are subject to a diminished expectation of loyalty.

The fact that a conflicted fiduciary is subject to a more demanding standard of loyalty does not mean that the beneficiary enjoys a higher right or more generous menu of remedies where the standard is violated.

The constructive trust is a controversial remedy because of its third party effects. Wherever a beneficiary seeks a proprietary remedy such as the constructive trust, he must be able to establish the right kind of connection between the wrong he has suffered and the form of relief claimed. I have argued that the majority of the Supreme Court was right to conclude that a constructive trust was not available to remedy the breach in *Indalex*. Nonetheless, the Court did not adequately justify its conclusion. Expanding on the test laid down in *Soulos*, I explained the kind of connection between wrong and remedy needed for a constructive trust to be an appropriate remedy for fiduciary disloyalty.

I will conclude by noting some jurisprudential lessons that may be drawn from *Indalex*. Fiduciary theorists have recently been engaged in lively debate over foundational elements of fiduciary liability. Amongst other matters, there is debate over the form and content of fiduciary loyalty norms (e.g., whether these norms are entailments of virtue or duty, whether they express a single overarching concept of loyalty or various conceptions of loyalty, and so on). There is also debate over the nature, function and justification of various fiduciary remedies (e.g., whether restitutionary remedies serve a public deterrence function or purely private remedial or attributive functions). *Indalex* offers nourishing food for thought on these questions.

In terms of fiduciary loyalty norms, *Indalex* suggests rather powerfully that the content of the duty of loyalty is variable.⁹¹ The proscriptive rules are default standards of fiduciary loyalty, but they cannot be exhaustive of fiduciary loyalty. It is important to note that while there is variation in standards of loyalty, the variation is not arbitrary. The *demonstrable partiality* standard operates alongside the *exclusive interest* standard reflected in the proscriptive rules. Nevertheless, partial suspension of the proscriptive rules means that whatever concept of loyalty one might invoke to explain fiduciary loyalty, it cannot be premised on the notion that loyalty is invariably a jealous or exclusive form of partiality. The *demonstrable partiality* standard suggests that one can have multiple and non-exclusive loyalties without the quality of a fiduciary's commitment to the beneficiary being diminished. Multiple loyalties may be more fragile than exclusive ones, but they are not incoherent as such.

91. As suggested by Gold, "Loyalties", *supra* note 9.

As for remedies, *Indalex* gives reason to question the argument that restitutionary remedies for breach of fiduciary duty have a purely deterrent purpose. It is sometimes said that remedies like constructive trusts and disgorgement awards are, or should be, broadly available to limit the socially pernicious effects of fiduciary infidelity.⁹² On this view, restitutionary remedies are awarded for reasons of public policy only contingently connected with primary rights generated by fiduciary relationships. As others have carefully explained, this is a rather artificial way of looking at things.⁹³ By focusing squarely on the connection between wrong and remedy, the majority of the Court in *Indalex* lent support to the view that restitutionary remedies vindicate claims to gains that belong to beneficiaries as a matter of primary right. If the beneficiary's right to loyalty does not extend to an asset claimed via constructive trust, her claim to the asset *in specie* ought not to be recognized, no matter how meritorious her claim or how damnable the conduct of the fiduciary in light of morality and public policy.

92. See e.g. John D McCamus, "Remedies for Breach of Fiduciary Duty" in Law Society of Upper Canada, ed, *Fiduciary Duties: Special Lectures of the Law Society of Upper Canada, 1990* (Toronto: Richard De Boo, 1991) 57; Robert H Sitkoff, "An Economic Theory of Fiduciary Law" in Gold & Miller, *supra* note 3, 197.

93. L Smith, "Deterrence, Prophylaxis and Punishment", *supra* note 62.

