

Fiduciary Duties, Conflict of Interest, and Proper Exercise of Judgment

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Résumé de l'article

L'un des problèmes les plus importants de la théorie du droit fiduciaire est la méconnaissance des implications qui découlent d'une situation de conflit d'intérêts. La littérature juridique contemporaine dominante sur les obligations fiduciaires repose sur le double postulat que, d'une part, les humains sont enclins à agir dans leur propre intérêt et, d'autre part, ils sont trop faibles pour résister à cet instinct de façon consciente tout en ayant l'obligation d'administrer les intérêts d'une autre personne. Bien que ces postulats puissent être fondés dans de nombreux cas de violation des obligations fiduciaires, ils ne suffisent pas à expliquer pourquoi des obligations fiduciaires sont imposées dans des situations où la bonne foi et l'honnêteté d'un fiduciaire ne sont pas remises en question. Cet article propose une nouvelle conception de la notion de conflit d'intérêts. Utilisant des notions provenant de la psychologie cognitive, de l'économie comportementale et de la philosophie, cet article définit un conflit d'intérêts comme une situation dans laquelle une personne, ayant le devoir d'exercer son jugement pour le profit d'autrui, a un intérêt qui tend à interférer avec le bon exercice de son pouvoir discrétionnaire. La théorie émergente et interdisciplinaire sur les conflits d'intérêts démontre que les intérêts personnels ou externes interfèrent avec le jugement d'un décideur de façon imprévisible, malgré les efforts honnêtes du décideur de les tenir à l'écart. Cette théorie propose une justification plus probante pour la nature stricte des régimes actuels de responsabilité fiduciaire. Elle offre également un argument robuste contre les demandes récentes d'assouplir ce régime fiduciaire strict dans des contextes commerciaux.

FIDUCIARY DUTIES, CONFLICT OF INTEREST, AND PROPER EXERCISE OF JUDGMENT

*Remus Valsan**

One of the foremost problems of fiduciary law theory is the imprecise understanding of what a situation of conflict of interest involves. The mainstream contemporary legal literature on fiduciary duties is premised on the dual assumption that, on the one hand, humans are inclined to act self-interestedly and, on the other hand, they are too weak to consciously resist this urge while managing another person's interests. Although these assumptions may be true in many cases of breach of fiduciary duties, they do not suffice to explain why fiduciary duties are imposed in situations where a fiduciary's good faith and honesty cannot be questioned. This article proposes a novel understanding of the notion of conflict of interest. Building on insights from cognitive psychology, behavioural economics, and philosophy, this article defines a conflict of interest as the situation where a person, who has a duty to exercise judgment for the benefit of another, has an interest that tends to interfere with the proper exercise of his or her discretion. The emerging interdisciplinary theory of conflicts of interest shows that personal or extraneous interests interfere with a decision maker's judgment in unpredictable ways, despite the decision maker's honest efforts to keep them aside. This theory offers a more persuasive rationale for the strictness of fiduciary liability. It also offers a potent argument against the recent calls to relax the strict fiduciary regime in commercial contexts.

L'un des problèmes les plus importants de la théorie du droit fiduciaire est la méconnaissance des implications qui découlent d'une situation de conflit d'intérêts. La littérature juridique contemporaine dominante sur les obligations fiduciaires repose sur le double postulat que, d'une part, les humains sont enclins à agir dans leur propre intérêt et, d'autre part, ils sont trop faibles pour résister à cet instinct de façon consciente tout en ayant l'obligation d'administrer les intérêts d'une autre personne. Bien que ces postulats puissent être fondés dans de nombreux cas de violation des obligations fiduciaires, ils ne suffisent pas à expliquer pourquoi des obligations fiduciaires sont imposées dans des situations où la bonne foi et l'honnêteté d'un fiduciaire ne sont pas remises en question. Cet article propose une nouvelle conception de la notion de conflit d'intérêts. Utilisant des notions provenant de la psychologie cognitive, de l'économie comportementale et de la philosophie, cet article définit un conflit d'intérêts comme une situation dans laquelle une personne, ayant le devoir d'exercer son jugement pour le profit d'autrui, a un intérêt qui tend à interférer avec le bon exercice de son pouvoir discrétionnaire. La théorie émergente et interdisciplinaire sur les conflits d'intérêts démontre que les intérêts personnels ou externes interfèrent avec le jugement d'un décideur de façon imprévisible, malgré les efforts honnêtes du décideur de les tenir à l'écart. Cette théorie propose une justification plus probante pour la nature stricte des régimes actuels de responsabilité fiduciaire. Elle offre également un argument robuste contre les demandes récentes d'assouplir ce régime fiduciaire strict dans des contextes commerciaux.

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Introduction

John Byng was a well-reputed admiral of the English Royal Navy. In 1756, he was defeated by the French naval fleet in the battle for the Mediterranean island of Minorca. Although Admiral Byng had notified his superiors of the multiple causes of his failure (including insufficient military personnel, damaged ships, and failed communications), public outrage demanded that Byng bear the blame. The following year, Byng was court-martialed, accused of “not do[ing] his utmost” to prevent Minorca from falling to the French navy, and executed by firing-squad.¹ Byng’s scapegoat execution led Voltaire to remark sarcastically: “[D]ans ce pays-ci [l’Angleterre] il est bon de tuer de temps en temps un amiral, pour encourager les autres.”²

Surprisingly, the practice that triggered Voltaire’s ridicule more than two centuries ago is nowadays invoked by courts and established fiduciary law scholars as the main justification for the onerous proscriptive duties that bind persons occupying a fiduciary position. In a recent decision of the England and Wales Court of Appeal, for example, Lady Justice Arden explained the severity of the proscriptive fiduciary duties by invoking the need to discipline fiduciaries, Admiral Byng-style:

It may be asked why equity imposes stringent liability ... [E]quity imposes stringent liability on a fiduciary as a deterrent—pour encourager les autres. ... [I]n the interests of efficiency and to provide an incentive to fiduciaries to resist the temptation to misconduct themselves, the law imposes exacting standards on fiduciaries and an extensive liability to account.³

The view that strict duties are necessary in order to deter and discipline all fiduciaries is very common in fiduciary law literature. Robert Flannigan, for instance, contends that only an indiscriminating “sledgehammer” approach to conflicts of interest can eliminate fiduciaries’ incentives for opportunistic manipulation.⁴ Gareth Jones, another outstanding equity scholar, has a similar, although more nuanced, view.

¹ Peter Burke, *Celebrated Naval and Military Trials* (London: WH Allen, 1866) at 60–92 (quotation at 80).

² “In this country [England], it is advisable to kill an admiral from time to time to set an example for the others” (Voltaire, “Candide, ou l’optimisme” in Voltaire, *Romans* (Paris: Firmin Didot Frères, 1851) 113 at 172 [translated by author]). See also Burke, *supra* note 1 at 86.

³ *Murad v Al-Saraj*, [2005] EWCA Civ 959 at para 74, [2005] All ER (D) 503 [*Murad*].

⁴ Robert Flannigan, “The Strict Character of Fiduciary Liability” [2006] 2 NZLR 209 (“[o]ur sledgehammer is designed to ‘encourager les autres’ generally (rather than selectively or sporadically) to give up *any* thought of unauthorized gain from manipulating the appearance of transactions or relations” at 217 [emphasis in original]).

He argues that, exceptionally, courts should be able to compel honest fiduciaries to disgorge unauthorized gains in order to punish them, *pour encourager les autres*.⁵

The argument that the law must impose onerous proscriptive duties on all fiduciaries, regardless of their honesty, in order to deter them from succumbing to the temptation of easy gains is counterintuitive and cannot be easily accommodated within many influential frameworks of private law. This article offers a novel justification for the peculiar strictness of fiduciary duties, which is based on a more precise understanding of the notion of conflict of interest. The starting point of many fiduciary theories is that, because the fiduciary has scope for the exercise of power or discretion and is tempted to act self-interestedly, her self-regarding interests come into conflict with the beneficiary's interests. Yet, equating this understanding of conflicting interests with the notion of conflict of interest is an error that has obstructed efforts to identify the proper role of the proscriptive duties and the underlying core features of all fiduciary relationships.

Building on insights from cognitive psychology, behavioural economics, and philosophy, this article defines a conflict of interest as a situation in which a person, who has a duty to exercise judgment for the benefit of another, has an interest that tends to interfere with the proper exercise of her discretion. Conflict of interest situations affect the reliability of the decision maker's judgment in ways that cannot be measured or corrected adequately. This theory offers a sound explanation for the peculiar harshness of fiduciary duties. The central reason for the strictness of fiduciary duties is not to prevent the temptation to steal or shirk, or to discipline the market, as the prevailing justifications hold, but rather to prevent self-interest or other-regarding interests from interfering with the fiduciary's core duty to exercise judgment based on relevant considerations. The proscriptive duties thus protect the beneficiary's right to the fiduciary's best judgment by preventing self-interest or other-regarding interests from interfering with the fiduciary's proper exercise of judgment.

The article proceeds as follows. Part I outlines the current legal framework of fiduciary duties, with a focus on the content of these duties and the shortcomings of the main theoretical justifications for their strictness (namely, the deterrence and vulnerability arguments).⁶ Deter-

⁵ See Gareth Jones, "Unjust Enrichment and the Fiduciary's Duty of Loyalty" (1968) 84:4 Law Q Rev 472 at 487.

⁶ The analysis in this article draws mainly on Canadian and British case law, with occasional references to Australian and American decisions. The decisions of the Supreme Court of Canada are highly relevant since this court has played a key role in the development of the fiduciary law and jurisprudence in Canada and beyond. The British prec-

rence and vulnerability are unconvincing explanations because they misunderstand what lies at the core of a conflict of interest situation. That is, they focus on the opposing interests between the parties to a fiduciary relationship, rather than on the conflict between the fiduciary's interests and her core fiduciary duty to exercise proper judgment. Part II shows that the current misunderstanding of what a conflict of interest situation entails goes back to the early stages in the development of fiduciary law. It will also show that the notion of conflict of interest proposed in this article existed in the early stages of fiduciary jurisprudence, but was eventually overshadowed by the conflicting interests justification of the strictness of fiduciary duties. Part III demonstrates that the emerging interdisciplinary theory of conflicts of interest validates the notion of conflict of interest put forward in this article. The danger of a conflict of interest situation, the emerging theory shows, resides in the risk of unreliable judgment caused by self-interest, rather than the risk of opportunism. Part IV applies this insight to fiduciary law, and presents the positive and normative consequences of our definition of conflicts of interest to fiduciary conflicts of interest. The new theory advances fiduciary law theory in three respects. First, it shows that the core fiduciary duty of proper judgment is essential to understanding the rationale underlying the strictness of prescriptive duties. Second, it provides cogent arguments against recent calls to relax the no-conflict and no-profit rules. Third, it argues that the focus of fiduciary jurisprudence should shift from instructing fiduciaries to resist temptation, to developing effective mechanisms to manage conflict of interest situations.

I. The Dominant View on the Content and Rationale of Fiduciary Duties

Fiduciary duties exert on common law scholars “something of the fascination ... that the search for the Holy Grail had for the knights of antiquity.”⁷ Like the quest for the Holy Grail, the search for the nature and content of fiduciary duties has been complicated by the fact that scholars disagree on what precisely the expression “fiduciary duty” means.⁸

This Part briefly surveys the main theories concerning the content of fiduciary duties and the principal justifications for their existence. The

edents are important for understanding the foundation on which the Canadian fiduciary law is built.

⁷ Donovan Waters “Banks, Fiduciary Obligations and Unconscionable Transactions” (1986) 65:1 Can Bar Rev 37 at 56.

⁸ See e.g. RP Austin, “Moulding the Content of Fiduciary Duties” in AJ Oakley, ed, *Trends in Contemporary Trust Law* (Oxford: Clarendon Press, 1996) 153 at 153; The Hon Dyson Heydon QC, “Modern Fiduciary Liability: The Sick Man of Equity?” (2014) 20:10 Trusts & Trustees 1006 at 1007.

dominant theory that has emerged across common law jurisdictions is that fiduciary duties are a set of proscriptive duties that aim at preventing certain private law actors from acting in their self-interest. This entrenched view of the content and purpose of fiduciary duties is a major obstacle to creating a sound and principled foundation for the law of fiduciary duties. As will be shown below, the idea of discouraging the temptation of selfishness is intertwined with the concepts of deterrence and vulnerability, which are too broad and too vague to be effective hallmarks of the fiduciary relationship.

A. *When Do Fiduciary Duties Arise?*

Fiduciary duties arise in fiduciary relationships.⁹ Which relationships are viewed in law as having a fiduciary character has been a contentious question for many decades. Historically, only a limited number of relationships were recognized by courts as fiduciary,¹⁰ but this traditional, narrow approach has been gradually loosened. Today, courts and commentators across common law jurisdictions recognize that fiduciary relationships are not restricted to powers over another's property, and that the list of fiduciary relationships is not closed.¹¹

The recognition of the open-ended nature of fiduciary relationships has created the need to identify the core elements that trigger the application of fiduciary duties in new relationships. The problem of identifying the core elements of a fiduciary relationship has been amply debated and, until recently, there was no sign of progress in sight.¹² Recent jurispru-

⁹ See Paul B Miller, "The Fiduciary Relationship" in Andrew S Gold & Paul B Miller, eds, *Philosophical Foundations of Fiduciary Law* (Oxford: Oxford University Press, 2014) 63.

¹⁰ Established fiduciary positions initially included trustees, guardians, executors, agents, attorneys, corporate directors or officers, and partners (see Austin Wakeman Scott, "The Trustee's Duty of Loyalty" (1936) 49:4 Harv L Rev 521 at 521).

¹¹ Canadian courts and commentators are the champions of the open-ended nature of fiduciary relationships (see e.g. *Guerin v The Queen*, [1984] 2 SCR 335 at 384, 13 DLR (4th) 321; *Lac Minerals Ltd v International Corona Resources Ltd*, [1989] 2 SCR 574 at 597, 648, 61 DLR (4th) 14 [*Lac Minerals*]; *Cuthbertson v Rasouli*, 2013 SCC 53 at para 193, [2013] 3 SCR 341; Ernest J Weinrib, "The Fiduciary Obligation" (1975) 25:1 UTLJ 1 at 7). The context-driven approach to fiduciary relationships is not limited, however, to the Canadian common law (see e.g. *Hospital Products Ltd v United States Surgical Corporation*, [1984] HCA 64, [1984] 156 CLR 41 at 96, 102, 55 ALR 417 [*Hospital Products*]). See also LS Sealy, "Fiduciary Relationships" (1962) 20:1 Cambridge LJ 69 at 73.

¹² See e.g. Lionel Smith, "Fiduciary Relationships: Ensuring the Loyal Exercise of Judgment on Behalf of Another" (2014) 130:4 Law Q Rev 608 at 610 [Smith, "Judgment"]; PJ Millett, "Equity's Place in the Law of Commerce" (1998) 114:2 Law Q Rev 214 at 218–

dential developments, however, have focused the analysis on two elements: an undertaking to act for another, and the power or discretion to affect their interests.¹³ The requirement of undertaking to act for another signifies that fiduciary duties are triggered voluntarily. They are enforceable only against those persons who undertook to do something for the benefit of another person or for an abstract purpose.¹⁴ A discretionary power to affect the legal or practical interests of another is the second fundamental characteristic of fiduciary relationships. Although most scholars accept that fiduciaries have discretion,¹⁵ they interpret differently the meaning of this element and the way in which fiduciary duties control it.

Some scholars equate discretion with opportunities to cheat¹⁶ or to exploit other people's vulnerability,¹⁷ or with enlarged scope for fiduciaries to breach non-fiduciary duties.¹⁸ Therefore, in their view, fiduciary duties

19; Peter D Maddaugh, "Definition of Fiduciary Duty" in *Special Lectures of the Law Society of Upper Canada, 1990: Fiduciary Duties* (Scarborough: De Boo, 1991) 15 at 16.

- ¹³ See *Galambos v Perez*, 2009 SCC 48 at paras 66, 70, [2009] 3 SCR 247 [*Galambos*]; *Alberta v Elder Advocates of Alberta Society*, 2011 SCC 24 at para 36, [2011] 2 SCR 261; *Manitoba Metis Federation Inc v Canada (AG)*, 2013 SCC 14 at para 50, [2013] 1 SCR 623. Vulnerability is another element that is often regarded as an indicator of a fiduciary relationship. In contrast to undertaking and discretion, the relevance of vulnerability is highly controversial (see Part I-C-2, below).
- ¹⁴ See James Edelman, "When Do Fiduciary Duties Arise?" (2010) 126:2 Law Q Rev 302.
- ¹⁵ See e.g. Weinrib, "The Fiduciary Obligation", *supra* note 11; Matthew Conaglen, *Fiduciary Loyalty: Protecting the Due Performance of Non-Fiduciary Duties* (Portland, Or: Hart, 2010) at 247–49 [Conaglen, *Fiduciary Loyalty*].
- ¹⁶ This view is prevalent in the law and economics analysis of fiduciary relationships (see e.g. Anthony Duggan, "Contracts, Fiduciaries and the Primacy of the Deal" in Elise Bant & Matthew Harding, eds, *Exploring Private Law* (Cambridge: Cambridge University Press, 2010) 275 at 278–79).
- ¹⁷ See e.g. Tamar Frankel, "Fiduciary Law" (1983) 71:3 Cal L Rev 795 at 810; Leonard I Rotman, "Fiduciary Law's 'Holy Grail': Reconciling Theory and Practice in Fiduciary Jurisprudence" (2011) 91:3 BUL Rev 921 at 941–42. See also *Lac Minerals*, *supra* note 11 at 599; *Hodgkinson v Simms*, [1994] 3 SCR 377 at 467, 117 DLR (4th) 161 [*Hodgkinson*].
- ¹⁸ See e.g. Conaglen, *Fiduciary Loyalty*, *supra* note 15 at 248. The central thesis of Conaglen's theory is that the no-conflict and no-profit principles provide a subsidiary and prophylactic form of protection to non-fiduciary duties. They increase the likelihood of a proper performance of the non-fiduciary duties, by seeking to avoid influences or temptations that are likely to interfere with the proper performance of the fiduciary's non-fiduciary duties (*ibid*). It is submitted that this is a variant of the traditional conflicting interests approach, with which this author disagrees. For critiques of Conaglen's theory, see e.g. Rebecca Lee, "In Search of the Nature and Function of Fiduciary Loyalty: Some Observations on Conaglen's Analysis" (2007) 27:2 Oxford J Leg Stud 327; Deborah A DeMott, "Disloyal Agents" (2007) 58:5 Ala L Rev 1049 at 1057–58, nn 37–38; Joshua Getzler, "Am I My Beneficiary's Keeper? Fusion and Loss-Based Fi-

control discretion in the sense of removing temptations to gain unauthorized benefits. In my view, this understanding of discretion is erroneous. The decision of whether to misappropriate another's property or opportunities is not an exercise of discretion in any meaningful sense of the term. Exercising fiduciary discretion over another's interests means being in a position to adopt a decision on another person's behalf. The fiduciary does not face a single predetermined course of action, but rather a wide range of permissible options, within the objective limits of her powers.¹⁹ Moreover, a fiduciary's discretionary power is not simply a power to alter the beneficiary's legal position. Many people hold powers that affect the interests of others, without being bound by fiduciary duties in exercising them. Non-fiduciary or personal powers—such as the power of appointment held in personal, rather than fiduciary capacity, the power to renew or terminate unilaterally a contract, and the power to accelerate before repayment of a demand loan—change the legal position of others but are subject to less onerous obligations than fiduciary duties.²⁰

The discretionary fiduciary power is the authority to decide how to promote the best interests of the beneficiary, rather than simply the authority to decide whether to act in a predefined manner. In other words, the requirement of power is best understood as decision-making authority.²¹ Discretionary power, in this sense, is a feature of fiduciary relationships that is often acknowledged in the fiduciary law literature, but rarely fully grasped. A person having decision-making authority over the interests of another is bound by a core fiduciary duty to exercise this authority by taking into account relevant considerations and omitting irrelevant ones.²² She also becomes bound by the proscriptive duties, which protect the decision-making process from the interference of conflicting interests or duties. As explained in Parts I-B to I-D, the mainstream theory of fiduciary law focuses on the proscriptive duties independently of the decision-making feature of a fiduciary position. The failure to connect these two el-

duciary Remedies" in Simone Degeling & James Edelman, eds, *Equity in Commercial Law* (Sydney: Lawbook, 2005) 239 at 267, n 112.

¹⁹ See Smith, "Judgment", *supra* note 12 at 610; Paul B Miller, "A Theory of Fiduciary Liability" (2011) 56:2 McGill LJ 235 at 275 [Miller, "Fiduciary Liability"]. See also Remus Valsan, "Fiduciary Duties of Credit Brokers: *McWilliam v Norton Finance*" (2016) 20:1 Ed L Rev 99 at 103.

²⁰ See generally Geraint Thomas, *Thomas on Powers*, 2nd ed (Oxford: Oxford University Press, 2012) at 474.

²¹ See Miller, "Fiduciary Liability", *supra* note 19 at 272–75. See also Paul B Miller & Andrew S Gold, "Fiduciary Governance" (2015) 57:2 Wm & Mary L Rev 513 at 549 (extending this definition to governance-type relationships).

²² See Part IV-A, below, for more on this topic.

ements is the main cause of the persisting disagreements over the content and role of fiduciary duties.

B. What Are Fiduciary Duties?

What do fiduciary duties demand of a fiduciary? The content of fiduciary duties is a topic that has generated decades of debates and theories.²³

Under the narrow approach to the content of fiduciary duties, which is dominant in contemporary case law and commentary, fiduciary duties are restricted to the proscriptive duties.²⁴ The proscriptive duties are based on two main rules: the no-profit rule and no-conflict rule.²⁵ The no-profit rule forbids a fiduciary from retaining any unauthorized benefit acquired by virtue of her fiduciary position.²⁶ The no-conflict rule states that a fiduciary is not allowed to place herself in a position where her personal interest, or interest in another fiduciary capacity, conflicts or may conflict with her duty.²⁷

Under a second, broad approach, fiduciary duties comprise the proscriptive no-conflict and no-profit duties, as well as several prescriptive duties, such as the duty of good faith and the duty of confidence.²⁸ This

²³ For a review of the main theories, see Leonard I Rotman, *Fiduciary Law* (Toronto: Thomson Carswell, 2005); Conaglen, *Fiduciary Loyalty*, *supra* note 15; JC Shepherd, *The Law of Fiduciaries* (Toronto: Carswell, 1981).

²⁴ See Richard Nolan, “A Fiduciary Duty to Disclose?” (1997) 113:2 Law Q Rev 220 at 222; Millett, *supra* note 12 at 222–23.

²⁵ See John McGhee, ed, *Snell’s Equity*, 33rd ed (London: Sweet & Maxwell, 2015) at para 7-008; AJ McClean, “The Theoretical Basis of the Trustee’s Duty of Loyalty” (1969) 7:2 Alta L Rev 218 at 236; Conaglen, *Fiduciary Loyalty*, *supra* note 15 at 39–40. The self-dealing rule and the fair-dealing rule are often added to this list (see e.g. Lionel Smith, “The Motive, Not the Deed” in Joshua Getzler, ed, *Rationalizing Property, Equity and Trusts: Essays in Honour of Edward Burn* (London: LexisNexis UK, 2003) 53 at 55–56, n 12 [Smith, “The Motive”]).

²⁶ See e.g. *Parker v McKenna* (1874), LR 10 Ch 96 at 118 (CA), 31 LT 739 [*Parker*]; *Regal (Hastings) Ltd v Gulliver*, [1942] UKHL 1, [1967] 2 AC 134 at 144, [1942] 1 All ER 378 [*Regal*].

²⁷ See e.g. *Aberdeen Railway Company v Blaikie Brothers*, (1854) 1 Macq 461 at 471, [1843–60] All ER 249 (HL (Scot)) [*Aberdeen Railway*]; *Boardman v Phipps*, [1966] UKHL 2, [1967] 2 AC 46 at 69, [1966] 3 All ER 721 [*Boardman*].

²⁸ See e.g. PD Finn, *Fiduciary Obligations* (Sydney: Law Book, 1977). In a more recent study of fiduciary obligations, Finn appears to revisit his earlier view. With respect to the content of the fiduciary obligation, he states that the fiduciary principle is properly understood as limited to the duty of loyalty, which he equates with the strict proscriptive duties (see PD Finn, “The Fiduciary Principle” in TG Youdan, ed, *Equity, Fiduciaries and Trusts* (Toronto: Carswell, 1989) 1 at 27–28 [Finn, “Fiduciary Principle”]). This broad view is often criticized for confusing fiduciary duties with related but distinct doctrines (see e.g. Conaglen, *Fiduciary Loyalty*, *supra* note 15 at 214–44).

broad approach is flawed because it fails to identify a core feature or duty that applies only to fiduciary positions. Indeed, it is generally agreed that not all duties owed by a fiduciary are fiduciary duties.²⁹ Duties of good faith, care, confidentiality, or disclosure are often associated with a fiduciary position, but they apply to a wide spectrum of non-fiduciary legal actors as well.

A third approach, located in the middle ground, separates the duties specific to persons in a fiduciary position into two main groups. On the one hand, there are the traditional proscriptive duties. On the other hand, there is a core fiduciary duty binding on fiduciaries, referred to by certain scholars³⁰ as “the duty of loyalty,” which is distinct from the proscriptive duties and justifies their existence. The proscriptive duties are connected with the core fiduciary duty in the sense that they play a protective or prophylactic role: they aim at preventing violations of the fundamental fiduciary duty. The views differ, however, as concerns the content of the core fiduciary duty. This duty has been defined as the duty to act (or to refrain from acting) with the proper motive,³¹ the duty “to promote the interests of another with care and disinterestedly,”³² the duty to look after and advance the beneficiary’s interests,³³ or the duty “to further the beneficiary’s best interests.”³⁴

These theories, connecting the proscriptive duties to a core fiduciary duty, represent the only approach that can provide a cogent understanding of fiduciary relationships. Nevertheless, they appear to fall outside of the dominant understanding of the content of fiduciary duties. The main reason why these theories await due recognition is that they do not offer persuasive explanations as to *why* the core fiduciary duty requires the special protection of the prophylactic duties. The justifications proposed by these theories for the need of this enhanced protection—such as the need to protect the beneficiary, to maintain the appearance of propriety, or to bypass evidentiary difficulties concerning the fiduciary’s actual motive—resemble those of the strictly proscriptive approach, in the sense

²⁹ See e.g. *Lac Minerals*, *supra* note 11 at 597; *Wewaykum Indian Band v Canada*, 2002 SCC 79 at para 83, [2002] 4 SCR 245.

³⁰ See e.g. Smith, “The Motive”, *supra* note 25; Andrew Burrows, “We Do This at Common Law but That in Equity” (2002) 22:1 Oxford J Leg Stud 1; Deborah A DeMott, “Beyond Metaphor: An Analysis of Fiduciary Obligation” [1988] 5 Duke LJ 879 [DeMott, “Beyond Metaphor”].

³¹ See Lionel Smith, “Understanding the Power” in William Swadling, ed, *The Quistclose Trust: Critical Essays* (Portland, Or: Hart, 2004) 67 at 70.

³² Peter Birks, “The Content of Fiduciary Obligation” (2000) 34:1 Israel LR 3 at 35.

³³ See Burrows, *supra* note 30 at 8–9.

³⁴ DeMott, “Beyond Metaphor”, *supra* note 30 at 882.

that they are external to the core fiduciary duty. The theory developed in this article aims at filling this gap in our understanding of the content of fiduciary duties. Relying on an interdisciplinary view of conflicts of interest,³⁵ this theory will show that the proscriptive no-conflict and no-profit duties protect the duty to exercise judgment based on relevant considerations. As explained in Part IV-A below, the theory developed in this article regards the duty to exercise judgment based on relevant considerations as the core fiduciary duty.

Irrespective of their approach to the content of fiduciary duties, scholars are in agreement that the proscriptive duties are very strict. Indeed, the peculiar strictness of the proscriptive duties has been the leitmotif of fiduciary law since the earliest reported cases.³⁶ Throughout the centuries, courts have identified several facets of the strictness of the proscriptive duties. One facet is the reprehensibility of self-interested conduct. Fiduciaries have been held liable for the breach of the no-conflict rule not only in cases of an actual conflict between interest and duty, but also where a reasonable possibility of such a conflict arose.³⁷ In some cases, it has been argued that even the remote possibility of conflict is sufficient to find a breach.³⁸ Another manifestation of the strictness of the proscriptive duties is that a fiduciary's liability is not precluded in instances where she has acted honestly and in good faith, where the beneficiary has suffered no loss or has even obtained a benefit following the impugned transaction, or where the opportunity that the fiduciary has taken for herself is no longer available to the beneficiary.³⁹

C. *Why Are Fiduciary Duties So Strict?*

Within the confines of the dominant view of the content of fiduciary duties, the peculiar strictness of the proscriptive duties is difficult to justify. Why are the fiduciary's honesty and good faith irrelevant? Why are courts not even prepared to admit evidence that no harm was caused?

³⁵ This view is presented in Part III, below.

³⁶ See e.g. *Keech v Sandford*, [1726] EWHC Ch J76, Sel Ca t King 61 at 62, 25 ER 223 [*Keech*]; *Forbes v Ross* (1788), 2 Cox 113 at 116, 30 ER 52 (Ch); *Parker*, *supra* note 26 at 124–25; *Bray v Ford* (1895), [1896] AC 44 at 51, 12 TLR 119 (HL (Eng)).

³⁷ See e.g. *Aberdeen Railway*, *supra* note 27 at 471–72; *Bhullar v Bhullar*, [2003] EWCA Civ 424 at paras 27–28, 41–42, [2003] 2 BCLC 241.

³⁸ See e.g. *Boardman*, *supra* note 27 at 111. It is generally agreed, however, that for a potential conflict of interest to exist, there must be a reasonable possibility of such conflict, not a mere appearance of conflict (see Donovan WM Waters, Mark R Gillen & Lionel D Smith, *Waters' Law of Trusts in Canada*, 4th ed (Toronto: Carswell, 2012) at 932).

³⁹ See *Regal*, *supra* note 26 at 144; *Aberdeen Railway*, *supra* note 27 at 472; *Boardman*, *supra* note 27 at 116.

Why is a fiduciary in breach of duty when the beneficiary suffered no apparent loss, or even benefitted from the conflicted transaction? The most frequent justifications for the strict nature of fiduciary duties are the need to discourage the temptation of selfish behaviour in fiduciaries (the deterrence argument), and the need to protect particularly vulnerable persons against the abuse of their trust and confidence in others (the vulnerability argument). As this section shows, these explanations are unconvincing.

1. The Deterrence Argument

Deterrence is one of the most frequently invoked policy explanations for the strictness of the proscriptive duties, and yet, one of the weakest arguments. Only indiscriminate punishment of actual and potential situations of conflict of interest, it is argued, can annihilate fiduciaries' incentives to take their chances and pursue unauthorized benefits.⁴⁰ Moreover, the role of fiduciary law is not to achieve a balance between the parties to a fiduciary relationship, but rather to set an example and to encourage good behaviour, by insisting that nothing short of exemplary propriety on the fiduciary's part is allowed.⁴¹ Some authors have gone so far as to claim that fiduciary law is akin to the criminal law of theft or embezzlement, and should follow the latter's underlying policy.⁴²

The deterrence theory suffers from several major flaws.⁴³ From a historical point of view, it is open to debate whether a policy of disciplining fiduciaries was the main reason for the introduction of these strict proscriptive duties. The landmark fiduciary law cases of the nineteenth century showed little or no concern for tracing the origin of these rules. They focused, instead, on expanding them to persons in trust-like positions, and on restating the need to maintain their strictness.⁴⁴ The deterrence explanation of fiduciary duties also lacks a clear connection to the core fiduciary duty. Refraining from stealing, embezzling, or converting another's property is not a duty that one has by virtue of occupying a fiduciary posi-

⁴⁰ See Flannigan, *supra* note 4 at 217.

⁴¹ See Gary Watt, *Trusts & Equity*, 7th ed (Oxford: Oxford University Press, 2016) (stating that “[i]nsistence upon exemplary fiduciary propriety encourages other persons in positions of trust to fulfil the requirements of their office” at 321).

⁴² See Tamar Frankel, “Fiduciary Duties as Default Rules” (1995) 74:4 *Or L Rev* 1209 at 1213, 1225. See also Frank H Easterbrook and Daniel R Fischel, *The Economic Structure of Corporate Law* (Cambridge, Mass: Harvard University Press, 1996) at 92, 98.

⁴³ For a thorough rebuttal of the deterrence argument, see Lionel Smith, “Deterrence, Prophylaxis and Punishment in Fiduciary Obligations” (2013) 7:1 *J Equity* 87 [Smith, “Deterrence, Prophylaxis, Punishment”].

⁴⁴ See Part II, below, for a historical overview of these cases.

tion. It is a general duty binding on all legal actors. The enhanced probability for such acts to occur in a fiduciary relationship and the presumed irresistible temptation of self-interest motivating fiduciaries are not sufficient reasons to impose the particularly harsh proscriptive duties on these actors.⁴⁵ Furthermore, the deterrence argument does not explain why no inquiry is allowed into the fiduciary's motives or good faith, once a reasonable possibility of conflict has been found to exist. If the law aims at deterring fiduciaries from improperly using their powers, punishing an innocent fiduciary is not good deterrence. The "deterrence at all costs" approach would in fact produce the opposite results. Punishing the potentially innocent would signal to the guilty that what matters is not their actual guilt or innocence, but how their actions appear to the outside world.⁴⁶ Finally, the idea that fiduciary law aims at disciplining legal actors by deterring temptation sits ill with many influential private law theories.⁴⁷ Private law focuses primarily on the bilateral relationship between two legal subjects, not on the interests of the community as a whole.⁴⁸ Sound private law doctrine must approach this field from the inside, using a set of coherent fundamental legal concepts and a mode of reasoning typical to private law, rather than relying on a functionalist approach based on a set of extrinsic purposes.

2. The Vulnerability Argument

Another justification for the strict fiduciary duties is the need to protect the beneficiaries of fiduciary relationships, who are peculiarly vulnerable to abuse. In *Lac Minerals Ltd. v. International Corona Resources Ltd.*, for example, Justice Sopinka remarked that vulnerability is the single indispensable requirement for the imposition of fiduciary duties.⁴⁹ In *Hodgkinson v. Simms*, Justices Sopinka and McLachlin, dissenting, restated their view that vulnerability, in the sense of extreme reliance, is the central element that generates the fiduciary duty.⁵⁰ In their view,

⁴⁵ Many legal relationships exist where one party has direct access to another's assets, such as a deposit, a lease, or a bare trust. All these relationships create an opportunity for misuse of those assets, but generally, they do not attract the imposition of fiduciary duties.

⁴⁶ See Shepherd, *supra* note 23 at 144.

⁴⁷ See Smith, "Deterrence, Prophylaxis, Punishment", *supra* note 43 at 92–93.

⁴⁸ For a detailed analysis of the goals of private law, see Ernest J Weinrib, *The Idea of Private Law* (Cambridge, Mass: Harvard University Press, 1995).

⁴⁹ See *Lac Minerals*, *supra* note 11 at 599.

⁵⁰ See *Hodgkinson*, *supra* note 17 at 467.

strict proscriptive duties are imposed in order to protect the vulnerable party, who is “at the mercy” of the party holding the power.⁵¹

The vulnerability theory is a weak explanation for the proscriptive duties. This theory is too broad because it encompasses situations of vulnerability that are the focus of other doctrines. Indeed, the protection of the weak, vulnerable, or disadvantaged could be seen as a secondary objective of fiduciary law, but it is too general to signal the special nature of fiduciary duties.⁵² In *Galambos v. Perez*, Justice Cromwell, writing the unanimous decision, discarded the normative relevance of vulnerability. He emphasized that vulnerability may be relevant insofar as it results from the relationship which creates the fiduciary duty, but a pre-existing situation of vulnerability is not essential to identifying the existence of a fiduciary duty.⁵³ Protection of inherently vulnerable persons is the main concern of other legal doctrines, such as unconscionability, undue influence, or good faith.⁵⁴

It has also been argued that vulnerability is relevant only as a factor that flows from the fiduciary relationship, rather than as a pre-existing feature of the beneficiary.⁵⁵ This understanding of vulnerability is also too broad. In many legal relationships, one party is vulnerable to an opportunistic breach of promise by the other party. The degree of the promisee’s vulnerability is directly proportional to his need for specific performance and to the difficulty of obtaining a substitute.⁵⁶ Vulnerability to an opportunistic breach of contract, however, does not trigger superimposed fiduciary duties not to act self-interestedly.

⁵¹ *Ibid.*

⁵² See *ibid* at 405, La Forest J (observing that vulnerability is a common theme to a multitude of equitable doctrines, and thus is not “the hallmark of the fiduciary relationship”). See also *Hospital Products*, *supra* note 11 at 68, Gibbs CJ (arguing that the core reason for the existence of the principle is the “special vulnerability” of beneficiaries to abuse of power by fiduciaries); *ibid* at 97, Mason J (justifying the strictness of fiduciary duties on the basis of the vulnerability of the beneficiary).

⁵³ See *Galambos*, *supra* note 13 at para 68. See also *Lac Minerals*, *supra* note 11 at 662–63, where Justice La Forest, dissenting, argued that vulnerability could be a relevant circumstance only when determining if new classes of relationships should be taken to give rise to fiduciary obligations. In this sense, the vulnerability of the abstract class of beneficiaries of the obligation is a relevant consideration. Vulnerability cannot be a decisive element in finding a fiduciary obligation in a particular, ad hoc relation.

⁵⁴ See *Hodgkinson*, *supra* note 17 at 405–06. See also Finn, “Fiduciary Principle”, *supra* note 28 at 32; Jane Stapleton, “The Golden Thread at the Heart of Tort Law: Protection of the Vulnerable” (2003) 24:2 *Austl Bar Rev* 135.

⁵⁵ See Weinrib, “The Fiduciary Obligation”, *supra* note 11 at 6.

⁵⁶ See Daniel Friedmann, “The Efficient Breach Fallacy” (1989) 18:1 *J Leg Stud* 1 at 3, n 6.

3. An Evaluation of the Deterrence and Vulnerability Arguments

The shortcomings of the deterrence and vulnerability explanations of the strictness of fiduciary duties stem from their focus on the opposition between the individual interests of the fiduciary and those of the beneficiary. This understanding of fiduciary duties leaves unanswered the following fundamental question: what is so unique in the position of a fiduciary, that the law is concerned with removing the temptation of self-interest and with preserving the appearance of correctness? A proper understanding of the notion of conflict of interest, in the sense of the incompatibility between the core fiduciary duty to exercise judgment based on relevant considerations and adverse interests, is fundamental to finding cogent answers to this question.⁵⁷ As Part II will show, the idea that self-interest could affect a fiduciary's judgment was recognized in early fiduciary law theory. Unfortunately, commentators and judges lost sight of this conception of conflicts of interest as policy justifications for preserving the strictness of fiduciary duties gained primacy. These justifications highlighted the need to discourage fiduciaries from being tempted to abuse their position, and to overcome the evidentiary difficulties that courts could face in trying to uncover the existence or the extent of fiduciary wrongdoing. These elements pointed to the opposition between the interests of the fiduciary and those of the beneficiary. As conflict of interest (initially understood as a conflict between a fiduciary's duty and their self-interest) became synonymous with conflicting interests (opposing the interest of the beneficiary with that of the fiduciary), the core fiduciary duty to exercise judgment based on relevant considerations faded in the background. The theory developed in this article aims at resurrecting the core fiduciary duty, drawing on recent developments in the cognitive and behavioural sciences.

II. From Conflict between Interest and Duty to Conflicting Interests: A Historical Overview

As Part I has shown, the fiduciary nature of the proscriptive duties and their peculiar strictness are generally accepted features of fiduciary law. The meaning of conflicts of interest is the point with which the different approaches to the nature and content of fiduciary duties start to diverge.

⁵⁷ Very few contemporary fiduciary law scholars recognize that the essence of the no-conflict rule is the concern with reliable and unbiased judgment (see Smith, "Judgment", *supra* note 12 at 623–25; JE Penner, "Is Loyalty a Virtue, and Even If It Is, Does It Really Help Explain Fiduciary Liability?" in Gold & Miller, *Philosophical Foundations of Fiduciary Law*, *supra* note 9, 159 at 168–69).

In a loose, but frequent formulation, the term “conflict of interest” is used to refer to situations in which the fiduciary’s personal interest and the interest of the beneficiary point in opposite directions.⁵⁸ In a more precise approach, a conflict of interest is understood as the opposition between the fiduciary’s personal interest and her core fiduciary duty to exercise judgment based on relevant considerations. Very often, the duty side of the conflict of interest is interpreted broadly, as encompassing all duties that a fiduciary owes to the beneficiary. Consequently, although it refers to a conflict between interest and duty, this understanding of a conflict of interest is very similar to the conflicting interests approach: the conflict is between the fiduciary’s self-interest and her duty to the beneficiaries. The loose use of the term “conflict of interest” has obscured the existence of the core fiduciary duty and the purpose of the strict proscriptive duties.

The failure to properly understand the central conflict that is specific to persons in a fiduciary position is a chronic problem of fiduciary law. As will be discussed below, since the very early stages of the development of rules concerning trustees and other fiduciaries, judges and commentators have emphasized the need to preserve and enhance the disciplining effect of the proscriptive duties. Few jurists have probed deeper into the role that these duties serve in connection to a fiduciary’s essential role. Several scholars of the eighteenth century observed that the strict fiduciary prohibitions aim at preventing self-interest from distorting the fiduciary’s judgment. Consistent with the theory developed in this article, this conception of the purpose of fiduciary duties suggests that the essence of the current interdisciplinary view of conflicts of interest, which opposes extraneous interests and the proper exercise of judgment, was known to early fiduciary law scholars. Throughout the nineteenth century, however, this insight seems to have been lost, and public policy arguments became the most prominent justification for the need to control fiduciaries. As the focus shifted away from the need to ensure the proper exercise of judgment, to the need to prevent the temptation of abuse, courts and commentators referred to the conflict specific to persons in a fiduciary position in an imprecise manner, by using interchangeably the ideas of conflicting interests, and conflict between self-interest and core fiduciary duty.

⁵⁸ See e.g. Paul B Miller, “Justifying Fiduciary Remedies” (2013) 63:4 UTLJ 570 at 605. See also Irit Samet, “Guarding the Fiduciary’s Conscience: A Justification of a Stringent Profit-Stripping Rule” (2008) 28:4 Oxford J Leg Stud 763 at 765; Frankel, “Fiduciary Law”, *supra* note 17 at 811.

A. *Eighteenth-Century Justifications for the Strictness of the Proscriptive Duties*

Early references to the strict nature of fiduciary duties are vague or incomplete and do not allow a precise determination of the reason for their strictness. The need for deterrence, however, seems to be an underlying theme in the eighteenth-century sources.

*Keech v. Sandford*⁵⁹ is among the earliest cases that provide support for the deterrence argument. In this “extraordinarily cryptic case”,⁶⁰ Lord Keeper King emphasized that trustees are strictly prohibited from taking in their own name a lease no longer available to the beneficiary of the trust. The decision strongly cautions trustees against using the office they hold for their own benefit.⁶¹ The peculiar strictness of the proscriptive duties has two manifestations. First, Lord Keeper King argued that it is preferable to abandon a lease that could not be renewed for the benefit of the beneficiary, rather than to allow the trustee to take it in his own name. Second, a trustee who takes over such a lease is liable to hold it for the benefit of the beneficiary, even though he was not motivated by the desire to defraud the beneficiary.⁶²

In the absence of a more detailed reporting of this case, it is difficult to identify the rationale underlying the harshness of this rule binding trustees and other fiduciaries. The elusive reporting suggests that Lord Keeper King invoked deterrence not as an explanation for the establishment of the proscriptive duties, but rather as an important reason for the preservation of their strict character. His assertion that the

⁵⁹ *Supra* note 36.

⁶⁰ Joshua Getzler, “Rumford Market and the Genesis of Fiduciary Obligations” in Andrew Burrows & Alan Rodger, eds, *Mapping the Law: Essays in Memory of Peter Birks* (Oxford: Oxford University Press, 2006) 577 at 581 [Getzler, “Rumford Market”]. For historical insights into the rationale behind *Keech*, see generally Walter G Hart, “The Development of the Rule in *Keech v. Sandford*” (1905) 21:3 Law Q Rev 258; Stephen Cretney, “The Rationale of *Keech v. Sandford*” (1969) 33:3 Conveyancer & Property Lawyer 161; Dennis R Paling, “The Pleadings in *Keech v. Sandford*” (1972) 36:3 Conveyancer & Property Lawyer 159.

⁶¹ See *Keech*, *supra* note 36 at 62.

⁶² See *ibid*. The strict rule established in *Keech* was subsequently extended beyond leases, to a general prohibition from obtaining unauthorized benefits binding on persons in a fiduciary position. See Thomas Lewin, *A Practical Treatise on the Law of Trusts and Trustees*, 2nd ed (London: Maxwell & Son, 1842) at 179 (noting that any person who acquires an unauthorized pecuniary advantage “by the abuse of his fiduciary character” is liable to disgorge such profits); Frederick Thomas White & Owen Davies Tudor, *A Selection of Leading Cases in Equity*, 7th ed by Thomas Snow et al (London: Sweet & Maxwell, 1897) vol 2 at 695 (stating that *Keech* applies to any “person clothed with a fiduciary or quasi fiduciary character or position”).

“rule should be strictly pursued, and not in the least relaxed”⁶³ implies that, by the time of that decision, the prohibition of the pursuit of self-interest by trustees was already an established and rigid rule. Historically, however, the case has been received as establishing a preventive sanction that removes all incentives for a fiduciary to consider how he might gain from his position.⁶⁴

Another early use of the deterrence argument comes from Lord Kames. In his treatise on equity, Lord Kames argued that allowing trustees to draw direct or indirect benefits from their position would have “poisonous” consequences and would make trustees “lose sight of [their] duty.”⁶⁵ Although he stressed the dangers that self-interest poses to the trustee’s duty, Lord Kames did not elaborate on the particular duty that is susceptible to be breached by self-interest. He asserted, however, that the principle that prohibits trustees or tutors from purchasing property under their management was the same principle that prohibits persons occupying a judicial office from purchasing land that is subject to a lawsuit.

It is very likely that the principle to which Lord Kames alluded is the natural justice maxim that no person can be judge in his own cause (*nemo iudex in causa sua*). This maxim prohibits a person required to exercise impartial judgment from having a personal interest in the outcome of his decision.⁶⁶ The prohibition of being both judge and interested party in the same cause goes back to Roman times. Title 2 of Book 2 of the Theodosian Code, entitled “No person shall be judge in his own cause (Ne in sua causa

⁶³ *Keech*, *supra* note 36 at 62.

⁶⁴ See Getzler, “Rumford Market”, *supra* note 60 at 586. In *Whelpdale v Cookson*, Lord Chancellor Hardwicke made a similarly elusive reference to the core justifications of the strictness of the proscriptive rules, by invoking the need to prevent unwanted consequences and the evidentiary difficulties related to proving the fraud ((1747), 1 Ves Sen 9 at 9, 27 ER 856 (Ch) [*Whelpdale*]). Likewise, in *Fox v Mackreth*, Lord Thurlow stated that, in cases where trustees acted honestly in self-dealing transactions, the proscriptive duties must be maintained based on “the rules of a Court of Equity, from general policy, and not from any peculiar imputation of fraud” ((1788), 2 Cox 320 at 327, 30 ER 148 (Ch)).

⁶⁵ Lord Henry Home Kames, *Principles of Equity*, 2nd ed (London & Edinburgh: A Millar & A Kincaid & J Bell, 1767) vol 2 at 255.

⁶⁶ See *Hall v Harding* (1769), 4 Burr 2426 at 2431, 98 ER 271 (KB) (“when the question depends upon ... a matter of judgment, the party interested can never be a competent judge in his own cause”). See also John Erskine, *An Institute of the Law of Scotland*, vol 1 (Edinburgh: Bell & Bradfute, 1824) at 45 (“[d]eclinature is founded ... *ratione suspecti iudicis*, where either the judge himself, or his near kinsman, hath an interest in the suit. It is a rule founded in nature itself, [t]hat no man ought to judge in his own cause; and it holds, though the judge have only a partial interest in the cause”).

quis judicet),” states that “no person shall act as judge for himself.”⁶⁷ This prohibition was further popularized in the seventeenth century by Sir Edward Coke,⁶⁸ and was invoked again by several other treatises and court decisions in the late eighteenth century as the core justification for the proscriptive fiduciary rules. John Erskine, for example, provided a similar explanation for the civil law rule that prohibits tutors and curators from obtaining a personal benefit in relation to their position:

Neither tutors nor curators can be *auctores in rem suam*. They cannot, contrary to the nature of their trust, interpose their authority to any deed of the minor, in which themselves have an interest, or which tends to produce an obligation against him in their own favour, *more than they can be judges or witnesses in their own cause*.⁶⁹

Just like Lord Kames, Erskine connected the strict prohibition of self-interest with the established natural law prohibition of being both judge and party in the same cause, without further explaining how the natural law maxim applies to fiduciary positions.⁷⁰

The *nemo iudex* maxim was thus well-known to eighteenth-century jurists. It was regarded as a general rule of law, founded on nature and known to all legal systems.⁷¹ As part of natural justice, the maxim was

⁶⁷ *The Theodosian Code and Novels and the Sirmondian Constitutions*, translated by Clyde Pharr with the collaboration of Theresa Sherrer Davidson & Mary Brown Pharr (Princeton: Princeton University Press, 1952) at 39. The official interpretation of this text underlines that the reason why a person cannot be judge in a matter in which he is interested is the same reason that prohibits a person from being a witness in a case where he has an interest (*ibid* at 40).

⁶⁸ See Sir Edward Coke, *The First Part of the Institutes of the Lawes of England or a Commentarie upon Littleton: Not the Name of a Lawyer Onely, but of the Law it selfe*, 1st ed (London: Societie of Stationers, 1628) at 141. See also *Dr Bonham's Case* (1610), 8 Co Rep 113b at 118a, 25 ER 646. For a longer history of this maxim, see DEC Yale, “*Iudex in Propria Causa: An Historical Excursus*” (1974) 33:1 Cambridge LJ 80.

⁶⁹ Erskine, *supra* note 66 at 176 [emphasis added]. See also *Aitken v Hunter* (1871), 9 Macph (3d) 756 at 762 (Ct Sess), Lord Neaves (stating that no fiduciary is allowed to become *auctor in rem suam*). The *auctor in rem suam* and the *nemo iudex* rules share the same underlying rationale, namely the prohibition to act both as judge and party in the same cause (see Patrick Fraser, *A Treatise on the Law of Scotland Relative to Parent and Child and Guardian and Ward*, 2nd ed by Hugh Cowan (Edinburgh: T & T Clark, 1866) at 279).

⁷⁰ See also *York Buildings Company v Mackenzie* (1795), 8 Bro PC 42, 3 ER 432 (HL (Eng)) [cited to Bro PC], another early landmark fiduciary law decision that connects the strict prohibition of self-dealing by trustees with the *nemo iudex* rule (“[t]he ground on which the disability or disqualification rests, is no other than that principle which dictates that a person cannot be both judge and party” at 63 [emphasis added]).

⁷¹ See e.g. *Gibbons v Bishop of Cloyne* (1705), Holt KB 599 at 601, 90 ER 1232 (“[l]astly, here the bishop was both Judge and party, which is not to be allowed by any law in the world”); Stewart Kyd, *A Treatise on the Law of Awards* (Philadelphia: William P Farrant & Co, 1808) at 71 (“[i]t is a general rule of law, founded on the first principles of

firmly established in the context of judicial decision-making, where it embodied the principle that a person adjudicating should be disinterested and unbiased.⁷² The role of this maxim in the context of fiduciary duties, however, is less clear. Due to the scarcity of extant sources, it is difficult to draw firm conclusions on the relevance of the *nemo iudex* maxim as a justification for the strict nature of proscriptive duties. Subsequent cases have emphasized the danger of the temptation to act self-interestedly, but have lost sight of the knowledge that temptation must be avoided in order to ensure proper judgment.

B. Nineteenth-Century Justifications for the Strictness of the Proscriptive Duties

The need to preserve the strict nature of the proscriptive duties, largely for procedural reasons, is the dominant theme in nineteenth-century sources. The idea that strict proscriptive duties are needed in order to protect the core fiduciary duty is only sporadically mentioned. The decisions issued by Lord Eldon at the beginning of the nineteenth century have played a key role in the establishment of the “danger of temptation”, “security against discovery” and “primacy of principle” themes as the most prominent justifications for the proscriptive duties.⁷³

In *Ex parte Lacey*,⁷⁴ Lord Eldon asserted that assignees under a commission of bankruptcy cannot purchase an interest in the bankrupt’s estate sold under the commission. This prohibition does not depend on the morality of a particular transaction, but rather rests on the general principle that fiduciaries cannot do “any thing for their own benefit,” irrespective of the apparent honesty of the transaction.⁷⁵ This general principle is justified by the difficulty of proving the actual fairness of each transaction in which the fiduciary has a personal interest. Consequently, for policy

natural justice, that a man cannot be judge in his own cause”). See also *Mersey Docks Trustees v Gibbs* (1866), LR 1 HL 93 at 110, (1866) 30 JP 467 (“[i]t is contrary to the general rule of law, not only in this country, but in every other, to make a person judge in his own cause”).

⁷² See Lord Woolf et al, *De Smith’s Judicial Review*, 7th ed (London: Sweet & Maxwell, 2013) at 536–38.

⁷³ These ideas also appear in *Lister v Lister* (1802), 6 Ves Jr 631 at 632–33, 31 ER 1231 (Ch), where Sir W. Grant, Master of the Rolls, asserted that the no-conflict rule “is a rule of general policy, to prevent the possibility of fraud and abuse; for it may not always be possible to know, whether the property was undersold.”

⁷⁴ (1802), 6 Ves Jr 625, 31 ER 1228 (Ch) [cited to Ves Jr].

⁷⁵ *Ibid* at 629.

reasons, transactions that are not morally reprehensible must be sacrificed in order to ensure the effectiveness of the principle.⁷⁶

In *Ex parte James*, Lord Eldon reiterated the view that purchases by trustees of property under their administration should be strictly prohibited in all instances, irrespective of the trustee's honesty and regardless of whether the trustee has obtained an advantage from the sale.⁷⁷ By virtue of their position, trustees acquire detailed knowledge of the value of the property they administer, which puts them in a strategic position to use this information for their own benefit while maintaining the appearances of fairness. Consequently, a strict deterrent principle is required for all trustees, even if, in some cases, the application of this principle may cause losses to the beneficiaries of the trust. The evidentiary difficulties surrounding the establishment of the fiduciary's wrongdoing and the policy of deterrence are thus combined to justify the strictness of the proscriptive duties.⁷⁸ The only scenario in which courts are willing to scrutinize the merits of a transaction in which a trustee, in his private capacity, acquires a benefit in relation to the trust property, is if the trustee resigns his office with the beneficiary's free and fully informed consent.⁷⁹

In *Ex parte Bennett*,⁸⁰ Lord Eldon observed that the no-profit rule does not depend on an actual benefit accruing to trustees and other fiduciaries. Any possibility of benefit must be removed due to the courts' limited fact-finding powers and to protect "the safety of mankind."⁸¹ Beside his habitual arguments, Lord Eldon provided another explanation for the need to proscribe self-dealing. He observed that, due to "human infirmity", a trustee will not be able to prevent a personal interest from interfering with the optimal discharge of his duty.⁸² The meaning of "human infirmity" in this context is ambiguous. One potential interpretation is that humans do not have the capacity to gauge the effect that the existence of a personal interest has on the optimal exercise of their judgment.

Once it became settled that the absolute prohibition of self-interested acts has primacy over the actual circumstances of the case, courts refused to allow the fiduciary to raise the claim that the self-interested transac-

⁷⁶ See *ibid* at 627–28.

⁷⁷ See *Ex parte James* (1803), 8 Ves Jr 337 at 345, 348, 32 ER 385 (Ch).

⁷⁸ See *ibid* at 348–49.

⁷⁹ See *ibid* at 352–53.

⁸⁰ (1805), 10 Ves Jr 381, 32 ER 893 (Ch) [cited to Ves Jr].

⁸¹ *Ibid* at 385, 396 (quotation at 396).

⁸² *Ibid* at 394.

tion may be fair to the beneficiary. In *Wormley v. Wormley*,⁸³ Justice Johnson of the United States Supreme Court asserted that the issue of the fairness of a self-dealing transaction cannot be taken into account by the court:

[A] trustee shall not be permitted to mix up his own affairs with those of the *cestui que trust*. *Those who have examined the workings of the human heart*, well know, that in such cases, the party most likely to be imposed upon is the actor himself, if honest; and, if otherwise, that the scope for imposition given to human ingenuity, will enable it generally to baffle the utmost subtlety of legal investigation.⁸⁴

The language in *Wormley v. Wormley* suggests that the strict proscriptive rules are meant to prevent not only situations in which fiduciaries yield to temptation and use their human ingenuity to hide the unauthorized benefit from the eyes of the court, but also cases in which, due to the limitations of the human conscience or heart, self-interest tends to interfere with the proper discharge by a fiduciary of his duty. Such interference could be unintentional and perhaps unknown to the fiduciary.

In *Hamilton v. Wright*,⁸⁵ Lord Brougham underlined that the purpose of the rule against conflicts of interest is to curb the tendency of self-interest to interfere with the trustee's duty to the beneficiary:

There cannot be a greater mistake than to suppose ... that a trustee is only prevented from doing things which bring an actual loss upon the estate under his administration. It is quite enough that the thing which he does has a tendency to injure the trust; *a tendency to interfere with his duty*.⁸⁶

Regrettably, Lord Brougham's argument then shifted to the traditional justifications of the prohibition of self-interested acts. He referred to the need to prevent the trustee's misuse of information for his own benefit,

⁸³ 21 US (8 Wheat) 421 (1823).

⁸⁴ *Ibid* at 463 [emphasis added]. Justice Johnson's reference to "the workings of the human heart" may betray influences of natural law or natural justice philosophical ideas, where heart and conscience were closely linked concepts. On this notion, see generally Dennis R Klinck, *Conscience, Equity and the Court of Chancery in Early Modern England* (Farnham, Eng: Ashgate, 2010) at 199–201 (stating that the notions of heart, or conscience, are particularly associated with inward processes and dispositions that cannot be accessed or evaluated by external tribunals).

⁸⁵ (1842), 9 Cl & F 111, 8 ER 357 (HL (Eng)) [cited to Cl & F].

⁸⁶ *Ibid* at 123 [emphasis added]. See also Joseph Story, *Commentaries on Equity Jurisprudence as Administered in England and America*, 6th ed (Boston: Little & Brown, 1853) vol 1 at 361.

the court's inability to ascertain when such misuse occurs,⁸⁷ and the need to sacrifice potentially honest transactions in order to prevent the greater evil of undetected misbehaviour, without further clarifications concerning how self-interest tends to interfere with the trustee's duty.⁸⁸

The inadmissibility of any investigation into the actual fairness of a conflicted transaction ascribed a procedural nature to the proscriptive rules: whenever a conflict of interest existed, no further investigation into the substantial merits of the transaction was allowed or required.⁸⁹ The increasing emphasis on the procedural and inflexible nature of the proscriptive rules further overshadowed the primary reason for which they were established. Although some landmark decisions referred to the importance of precluding a conflict between interest and duty, the dominant explanation for the rigid proscriptive rules focused exclusively on the need to counteract the tendency inherent in human nature to yield to the temptation of selfishness.

The emphasis on the need to prevent self-interest led to a distortion of the idea of conflict of interest. Consequently, courts and commentators referred interchangeably to conflict between interest and duty, and conflicting interests without a clear understanding of the particular nature of the conflict that is specific to fiduciaries. This inappropriate understanding of the fiduciary conflict of interest appeared in the earliest treatises on equity. In his annotations to *A Treatise of Equity*, John Fonblanque emphasized that the strict prohibitions to which equity subjects trustees are meant to keep them "within the line of their duty" by preventing their personal interest from entering into conflict with that of the beneficiary.⁹⁰

Alternating references to conflict between interest and duty and conflicting interests are also found in *Aberdeen Railway Co v. Blaikie*

⁸⁷ The difficulties of proving a fiduciary's wrongdoing is an argument often invoked in the early fiduciary case law as a justification for maintaining the strictness of the fiduciary duties (see e.g. *Whelpdale*, *supra* note 64). This argument has lost its force over time. The modernization of civil procedure and the comprehensive requirements regarding appropriate recordkeeping by certain fiduciaries have alleviated to a great extent the evidentiary difficulty problem (see John H Langbein, "Questioning the Trust Law Duty of Loyalty: Sole Interest or Best Interest?" (2005) 114:5 Yale LJ 929 at 944–51).

⁸⁸ See *Hamilton v Wright*, *supra* note 85 at 123–24.

⁸⁹ See *Aberdeen Railway*, *supra* note 27 at 471–72. See also *Parker*, *supra* note 26 at 118.

⁹⁰ Henry Ballou, *A Treatise of Equity with the Addition of Marginal References and Notes by John Fonblanque*, vol 2, 4th ed by Antony Laussat (Brookfield, Mass: E & L Merriam, 1835) at 445. See also Thomas Lewin, *A Practical Treatise on the Law of Trusts and Trustees*, 1st American ed (Philadelphia: John S Littell, 1839) at 146–47; WM Bythewood, Thomas Jarman & George Sweet, *Bythewood & Jarman's System of Conveyancing: A Selection of Precedents in Conveyancing*, 4th ed by Leopold George Gordon Robins, vol 5 (London: H Sweet & Sons, 1888) at 96.

Brothers, one of the early landmark cases of fiduciary law, where Lord Cranworth famously stated that no fiduciary is allowed to have “a personal interest conflicting, or which possibly may conflict, with the interests of those whom he is bound to protect.”⁹¹ Shortly thereafter, he explained that the “very evil” which the strict no-conflict rule is designed to thwart is the situation in which a fiduciary acquires a personal interest that detracts from his duty.⁹² The idea that the proscriptive rules are the expression of a policy aimed at preventing fiduciaries from being tempted to act self-interestedly has survived to the present day as the most conspicuous explanation of the strictness of fiduciary duties.⁹³

C. Conflict between Interest and Core Fiduciary Duty in the Twentieth-Century Case Law

Although the conflicting interests understanding was prevalent in the twentieth century as well, the conception of conflict of interest as the opposition between extraneous interests and the duty to exercise proper judgment was not altogether absent from court decisions. Several judges and commentators have explained the irrelevance of the fiduciary’s good faith and desire to resist temptation in a situation of conflict of interest by underlining the insidious ways in which the possibility of self-interest may affect the fiduciary’s judgment. Similar to proponents of the contemporary interdisciplinary view of conflicts of interest, which will be explained in Part III, these jurists recognized that a situation of conflict risks compromising the fiduciary’s judgment in a way that cannot be measured or controlled.

In *Re Trusteeship of Stone*,⁹⁴ for example, Justice Zimmerman of the Supreme Court of Ohio observed that the reason why a trustee was in breach of duty of loyalty for self-dealing, although he acted in good faith, was the need to keep aside factors that tended to interfere with the reliability of his judgment:

[The self-dealing rule] may seem a harsh rule when applied to instances where there is no studied or deliberate design to do wrong and when the [investment activity] is conceived and executed in good faith. ...

⁹¹ *Aberdeen Railway*, *supra* note 27 at 471.

⁹² *Ibid* at 473.

⁹³ See e.g. Conaglen, *Fiduciary Loyalty*, *supra* note 15 at 73 (stating that the main aim of the no-conflict rule is to insulate the fiduciary from the temptation of acting self-interestedly).

⁹⁴ (1941), 34 NE (2d) 755, 138 Ohio St 293 (Sup Ct) [cited to NE (2d)].

[A fiduciary] must refrain from ... doing those things which would tend to interfere with the exercise of a wholly disinterested and independent judgment.⁹⁵

*Re Skeats's Settlement*⁹⁶ is one of the rare cases linking the *nemo iudex* rule with the idea of biased judgment. In this case, the donees of a fiduciary power granting them the authority to appoint “any other person” as trustee exercised the power to appoint themselves. Since the power was fiduciary in character, Justice Kay held that this exercise of discretion was invalid:

The universal rule is that a man should not be judge in his own cause; that he should not decide that he is the best possible person, and say that he ought to be the trustee. Naturally *no human being can be imagined who would not have some bias one way or the other as to his own personal fitness*, and to appoint himself among other people, or excluding them to appoint himself, would certainly be an improper exercise of any power of selection of a fiduciary character such as this is.⁹⁷

In a similar vein, Judge Earl R. Hoover, writing extra-judicially, explained that a fiduciary’s honesty and good intentions are no defence to a breach of the proscriptive duties, because “his judgment is so warped that he cannot be fair.”⁹⁸

As these examples illustrate, a precise understanding of the notion of conflict of interest, in the sense of an opposition between the decision maker’s personal interests and his exercise of judgment, is not altogether absent from the evolution of the fiduciary law. This understanding, however, has been obscured by the perceived need to prevent temptations of unauthorized benefits, and to protect vulnerable beneficiaries. Besides failing to acknowledge the biasing effect that extraneous interests have on a fiduciary’s judgment, the dominant theory of fiduciary obligations also obscures the fiduciary’s duty to exercise discretion based on relevant considerations. The prevention of a risk of bias and the duty to take into account relevant considerations are different facets of the same concern: the

⁹⁵ *Ibid* at 760 [emphasis added]. See also *Pyle v Pyle* (1910), 137 App Div 568 at 572, 122 NYS 256 (“[t]he purpose [of the no-profit and no-conflict rules] is to require a trustee to assume a position where his every act is above suspicion and the trust estate, and it alone, can receive not only his best services, but his unbiased and uninfluenced judgment”); *Thruston v Nashville & American Trust Co* (1940), 32 F Supp 929 at 936 (the proscriptive duties guarantee that fiduciaries “shall at all times have the benefit of the unbiased and disinterested judgment of the trustee”).

⁹⁶ (1889), 42 ChD 522, [1886–90] All ER 989 [cited to ChD].

⁹⁷ *Ibid* at 527 [emphasis added].

⁹⁸ Judge Earl R Hoover, “Basic Principles Underlying Duty of Loyalty” (1956) 5:1 Clev-Marshall L Rev 7 at 16.

protection of the beneficiary's right to the fiduciary's best judgment. Part III will show that this understanding of what defines a situation of conflict of interest, and of why it is dangerous for those exercising discretion over another's interests, is well established in the emerging interdisciplinary theory of conflicts of interest.

III. Conflict of Interest and Proper Exercise of Judgment: An Interdisciplinary Approach

The connection between self-interest and the proper exercise of discretion is a theme explored in depth by the emerging social sciences literature on conflicts of interest. Part II showed that this understanding of a fiduciary conflict of interest was known to the eighteenth- and nineteenth-century fiduciary lawyers. References to the *nemo iudex* rule and to the tendency of self-interest to influence the exercise of the fiduciary's duty seem to point to the same central idea: the mere presence of self-interest affects the proper exercise of judgment. Contemporary research into decision-making processes provides a more solid understanding of this phenomenon. Building on empirical studies, cognitive and behavioural researchers have contributed to the emergence of an interdisciplinary view of the notion of conflict of interest.

The interdisciplinary view is centred on the idea that the personal interests or preferences of a decision maker may affect the reliability and credibility of her judgment. Such interests or preferences interfere, consciously or unconsciously, with her ability to give fair and genuine consideration to factors that are relevant in adopting a decision. When a decision requires judgment, extraneous interests could undermine the decision-making process by reducing the reliability of the decision maker's judgment, without rendering it incompetent.

The interdisciplinary view of conflict of interest clarifies the mechanism of making decisions on another's behalf and offers valuable tools to advance the law of fiduciary duties. Building on consistent empirical evidence,⁹⁹ it demonstrates that personal interests tend to affect the decision-making process in ways that are beyond the decision maker's control, and indeed beyond any form of objective assessment.

⁹⁹ See Wayne Norman & Chris MacDonald, "Conflicts of Interest" in George G Brenkert, ed, *The Oxford Handbook of Business Ethics* (Oxford: Oxford University Press, 2009) 441 at 454.

A. *The Emergence of an Interdisciplinary Theory of Conflicts of Interest*

In the latter half of the twentieth century, a “minor revolution” took place in the understanding of conflicts of interest and the most appropriate strategies to manage them.¹⁰⁰ Breaking with the traditional ethical view, which advocated the resolution of conflicts between interest and duty by resisting the temptation of selfish acts, the new theory reveals that external interests can affect the judgment of even the most honourable and disciplined person. Consequently, the avoidance or management of conflict situations, rather than abstention from selfish acts, is the desirable course of action.

The traditional ethical view of conflict situations adopted a virtue-centric approach. A person faced with a choice between interest and duty was expected to do the right and honourable thing and resist the temptations of selfishness: “As long as this person has remained virtuous and fulfilled his primary duties, nothing morally wrong has happened.”¹⁰¹ The main flaw of this view is that it overestimates the ability of conflicted individuals to know if their judgment has been affected by the interfering interest. The interdisciplinary view overcomes this flaw by recognizing that a person is in a conflict of interest on the basis of being in a conflicted situation, irrespective of the person’s belief that she is capable of resisting the temptation or corrupting influence of the interest that could interfere with her judgment.¹⁰²

The traditional ethical view of conflict situations coincides with the dominant, narrow legal justification of fiduciary duties. In both fields, how a person responds to a situation of conflict tends to be regarded exclusively as a matter of incentives and conscious choice: the rightful course of action is to resist temptation, while the wrongful option is to act opportunistically.¹⁰³

¹⁰⁰ *Ibid* at 459.

¹⁰¹ *Ibid* at 447.

¹⁰² According to Norman & MacDonald, “[w]hat we now recognize is that [the traditional ethical view] is naïve: conflicted individuals can have their judgment interfered with even when they try their best to ‘correct’ for the influence of the conflicting interest ... In many cases, they may not even be aware of the influence some source of bias may have over them” (*ibid* at 461).

¹⁰³ See Don A Moore, Lloyd Tanlu & Max H Bazerman “Conflict of Interest and the Intrusion of Bias” (2010) 5:1 *Judgment & Decision Making* 37 at 46 [references omitted]:

[T]he mass media and the academic literatures in business, accounting, and law routinely assume that bias is a matter of deliberate choice. ...

[This] is challenged by psychological research which suggests that biased information processing is not only pervasive, but is typically unconscious and unintentional.

The interdisciplinary view of conflict of interest builds on recent developments in the cognitive sciences concerning decision-making processes. These developments suggest that interests affect “everything from the way individuals evaluate the seriousness of various risks and the desirability of particular outcomes, to the way they perceive connections between cause and effect.”¹⁰⁴ Consequently, conflict of interest situations are reprehensible not because they create a measurable bias, but rather because they raise an “unusual *risk* of error,”¹⁰⁵ thus rendering one’s judgment less reliable.¹⁰⁶

B. The Content of the Interdisciplinary Theory of Conflicts of Interest

The literature on cognitive and motivational biases provides detailed theoretical and empirical information on the ways in which personal interests can interfere with a person’s judgment. The interdisciplinary understanding of the ways in which interest affects judgment is based on a long-standing distinction drawn by psychologists between two different modes of information processing that characterize human cognition. On the one hand, there are automatic cognitive processes that are relatively effortless and unconscious. On the other hand, there are controlled processes that require more analysis and effort. Automatic and controlled processes often act in concert to produce judgments and decisions, but in certain predictable situations they can come into conflict.¹⁰⁷ In the case of professionals, the two different modes of reasoning govern two different sets of decisions. Decisions regarding professional responsibilities are governed by controlled processing, whereas decisions regarding personal interests are governed by automatic processing. As is the case of automatic and controlled processes, these motives often coincide and reinforce each other. When a conflict between professional duties and self-interest arises, the automatic mode of reasoning is likely to prevail. Consequently, self-

¹⁰⁴ Norman & MacDonald, *supra* note 99 at 454.

¹⁰⁵ Michael Davis, “Conflict of Interest” in Ruth Chadwick, ed, *Encyclopedia of Applied Ethics* (San Diego: Academic Press, 1998) vol 1, 589 at 589 [emphasis added] [Davis, “Conflict of Interest”].

¹⁰⁶ See Norman & MacDonald, *supra* note 99 (“conflicting personal and even professional interests can impair the judgment of even the most dedicated and conscientious expert” at 464). See also Don A Moore & George Loewenstein, “Self-Interest, Automaticity, and the Psychology of Conflict of Interest” (2004) 17:2 Social Justice Research 189 (arguing that, since “violations of professionalism induced by conflicts of interest often occur automatically and without conscious awareness,” a deterrent approach based on “the threat of legal punishments is a clumsy public policy” at 199).

¹⁰⁷ See Moore & Loewenstein, *supra* note 106 at 190.

interest is likely to influence professional judgment, even when a decision maker consciously attempts to comply with her duties.¹⁰⁸

The contemporary preoccupation with the appropriate understanding of a conflict of interest situation was triggered in early 1980s by the innovative work of Michael Davis.¹⁰⁹ The most relevant subsequent attempts to clarify this concept were framed explicitly in reaction to Davis' theory. As a result of these debates, several features of a conflict of interest situation have emerged as largely accepted, forming the basis of the interdisciplinary view of conflicts of interest.¹¹⁰ It should be noted that the main purpose of the interdisciplinary view is to determine the moral or ethical consequences of a conflict of interest. Fiduciary law theory, instead, is concerned with understanding the existing legal rules regulating conflicts of interest in private law. Despite its idiosyncratic objective, the interdisciplinary view can help legal scholars acquire an in-depth understanding of the ways in which a situation of conflict of interest affects the conflicted person.

The interdisciplinary view rejects as superficial the identification of a conflict of interest situation with the principal-agent problem,¹¹¹ which has dominated the philosophical and legal literature surrounding conflicts of interest in past decades. The principal-agent problem is premised on the conflicting interests approach discussed in Part II: because agents are rational utility maximizers, they seek to maximise their own utility, while only "satisficing" the principal's utility. Since it is costly or impracticable for the principal to closely monitor all of the agent's actions, the law must compel the agent to further exclusively the principal's interests.¹¹² The interdisciplinary view, in contrast, starts from the premise of a conflict between self-interest and professional duty. According to Davis,

A person has a conflict of interest if (a) he is in a relationship with another requiring him to exercise judgment in that other's service

¹⁰⁸ See *ibid* at 190–99.

¹⁰⁹ See Michael Davis, "Conflict of Interest" (1982) 1:4 *Business & Professional Ethics J* 17 [Davis, "Conflict"].

¹¹⁰ Michael Davis articulated the interdisciplinary view of conflict of interest (commonly referred to as "the standard view") based on the work of scholars from various fields, including philosophy, political theory, ethics, and law (see Michael Davis, "Introduction" in Michael Davis & Andrew Stark, eds, *Conflict of Interest in the Professions* (Oxford: Oxford University Press, 2001) 3 at 7–19 [Davis, "Introduction"]).

¹¹¹ See Norman & MacDonald, *supra* note 99 at 446.

¹¹² The principal-agent problem is the foundation of the law and economics, or contractarian, approach to fiduciary duties (see Frank H Easterbrook & Daniel R Fischel "Contract and Fiduciary Duty" (1993) 36:1 *JL & Econ* 425 at 427; Robert Cooter & Bradley J Freedman, "The Fiduciary Relationship: Its Economic Character and Legal Consequences" (1991) 66:4 *NYUL Rev* 1045 at 1047; Duggan, *supra* note 16 at 278–79).

and (b) he has an interest tending to interfere with the proper exercise of judgment in that relationship.¹¹³

Judgment is thus a central notion in the interdisciplinary view of conflict of interest: a decision maker's ability to exercise proper judgment is at risk of being compromised by a personal interest.¹¹⁴

The concept of judgment denotes the existence of discretion, in the sense of the absence of a predefined script or algorithm based on which a decision can be modelled. In a situation requiring the exercise of judgment, the specification of “the *problem* to be solved” or “the *ends* to be achieved” are contested, or open to interpretation.¹¹⁵ By contrast, decisions that do not require judgment “are ‘routine’, ‘mechanical’, or ‘ministerial’; they have (something like) an algorithm.”¹¹⁶ Ministerial decisions require only technical rationality. Specific theories or techniques are available to determine the most appropriate way to achieve predefined unambiguous goals.

Given the absence of a predefined pattern regarding the ends to be attained and the means to achieve them, the exercise of judgment goes beyond following mechanical rules.¹¹⁷ Judgment entails “knowledge, skill, and insight”, and the interactions of these factors can produce unpredictable results.¹¹⁸ When a decision requires judgment, different decision makers may disagree on the ends and the optimal course of action to be pursued, without anyone being wrong in an objective sense.¹¹⁹ In this scenario, a situation of conflict of interest impairs the decision maker's capac-

¹¹³ Davis, “Conflict”, *supra* note 109 at 21. Consider the following example:

I would ... have a conflict of interest if I had to referee at my son's soccer game. I would find it harder than a stranger to judge accurately when my son had committed a foul. ... I do not know whether I would be harder on him than an impartial referee would be, easier, or just the same. What I do know is that ... I could not be as reliable as an (equally competent) [referee] would be (Davis, “Introduction”, *supra* note 110 at 16).

¹¹⁴ See Norman & MacDonald, *supra* note 99 at 446, 455. See also W Bradley Wendel, “The Deep Structure of Conflicts of Interest”, Book Review of *Conflict of Interest in American Public Life* by Andrew Stark and *Conflict of Interest in the Professions* by Michael Davis & Andrew Stark, eds, (2003) 16:3 *Geo J Leg Ethics* 473 at 477; Dennis F Thompson, “Understanding Financial Conflicts of Interest” (1993) 329:8 *New Eng J Med* 573.

¹¹⁵ Wendel, *supra* note 114 at 479–80 [emphasis added].

¹¹⁶ Davis, “Conflict of Interest”, *supra* note 105 at 590.

¹¹⁷ See Davis, “Conflict”, *supra* note 109 (“[j]udgment implies discretion. ... A bank president does not need judgment to decide whether she (as president) should embezzle the bank's money. ... In contrast, a critic needs judgment to decide how good a play or actor is” at 22).

¹¹⁸ Davis, “Introduction”, *supra* note 110 at 8.

¹¹⁹ See *ibid.*

ity to evaluate the possible ends of judgment, but it does not affect her overall level of competence.

Extraneous interests interfere with judgment not as ends that a decision maker has in view, but as factors that tend to influence the ends in view.¹²⁰ In other words, the interdisciplinary view does not start from the proposition that a person who must exercise judgment for another yields to temptation and decides to pursue her own interests. It is premised instead, on the idea that the presence of such interests puts at risk the decision maker's ability to evaluate the weight to be given to the relevant considerations on which the decision is based.

Personal material interest provides the clearest example. The possibility of obtaining a personal unauthorized material gain as a result of a decision creates a situation of conflict, although the decision maker does not consciously pursue her own material interests. The mere presence of the possibility of such a benefit affects the reliability of the decision maker's evaluation of the relevant factors informing her decision. If a decision maker consciously acts with a view to obtaining an unauthorized benefit, not only does she exercise judgment inappropriately, she also steals or misappropriates.

Interest is another essential concept for the interdisciplinary view of conflicts of interest. Extraneous interests affect the decision-making process as factors that tend to influence the ends in view. Consequently, the extent of the effect of such interests on one's judgment cannot be assessed based on the actual decision taken. Because the decision maker is the person who is charged with deciding the appropriate course of action, one cannot simply measure the deviations from a "right" decision, which the interfering interest has caused.¹²¹ A decision adopted in a situation of conflict is inherently flawed, despite the conflicted person's willingness to put personal interests or ideological commitments aside. Since the effect of a conflict of interest cannot be assessed based on results, the theories of conflict of interest focus on certain kinds of identifiable interests that are particularly threatening to the exercise of judgment, such as material in-

¹²⁰ See *ibid* at 9.

¹²¹ Since interests affect judgment in unpredictable ways, courts are incapable of measuring the extent to which the decision maker's decisions deviate from the interests she was supposed to promote, or the extent to which the decision maker's judgment may have been impaired (see Andrew Stark, *Conflict of Interest in American Public Life* (Cambridge, Mass: Harvard University Press, 2000) at 21–22 (referring to judicial review of administrative decisions)).

terests or family ties. The categories of interfering interests, however, are not closed.¹²²

Although in the interdisciplinary view interest is an open-ended concept, it does not include just any factor that might compromise one's judgment. First, it excludes factors that may affect one's ability to use one's professional competence, such as loud noise or health problems.¹²³ Second, not all personal preferences can be set aside. Decision makers cannot be required or expected to transcend all aspects of their subjectivity and act like dehumanized, deciding machines. It is not psychologically feasible to divest oneself entirely of interests that are constitutive of one's personhood. Some subjective preferences may be harmless: not every decision that a person makes on another's behalf is influenced by every interest, and not every interest renders judgment unreliable.¹²⁴

A prohibition of all subjective beliefs, commitments, and loyalties is not only unfeasible, but also goes against the core idea of the exercise of discretion. The combination of personal characteristics that is specific to each decision maker accounts for the diversity of equally valid results that can flow from a situation involving discretion.¹²⁵ Consequently, a line must be drawn between legitimate factors that influence the decision maker's judgment and factors that have the ability to create a conflict of interest. According to Andrew Stark, the interests that should be encompassed by the notion of conflict of interest are those which exert a "normatively significant influence" on the decision maker's judgment.¹²⁶ Although what amounts to a normatively significant interest is open to debate, the interdisciplinary view seems to limit such interests to factors that are able to affect the reliability of a decision maker's judgment by their existence as potentialities. Ultimately, what constitutes a conflict of interest in a particular situation is an empirical question.¹²⁷ It is therefore not possible to draw an exhaustive list of relevant interests.

To summarize, the interdisciplinary view develops and clarifies the notion of conflict of interest in two main respects. First, it draws a clear line between relationships in which parties have conflicting interests, on the one hand, and situations in which an individual has a conflict between self-interest and professional duty, on the other hand. Indeed, situations in which parties have interests pointing in opposite directions are ubiqui-

¹²² See Davis, "Introduction", *supra* note 110 at 9–10.

¹²³ See *ibid* at 10.

¹²⁴ See Wendel, *supra* note 114 at 486.

¹²⁵ See *ibid* at 486–87.

¹²⁶ Stark, *supra* note 121, cited in Wendel, *supra* note 114 at 485.

¹²⁷ See Davis, "Introduction", *supra* note 110 at 10.

tous in markets for goods and services. They cannot be regarded as conflict of interest situations without rendering this concept excessively broad and useless. A conflict of interest arises in an individual, as an opposition between interest and duty, rather than between individuals. An individual is not conflicted because she has a personal interest in performing or abstaining from performing a duty that she owes to another. Such an understanding would also make the conflict of interest concept overly vague and meaningless. Properly understood, a conflict of interest opposes personal interest with the duty to exercise discretion over another's interests. In this scenario, interest and duty cannot be reconciled because extraneous interests affect the reliability of judgment in ways that cannot be measured or mitigated. Second, the interdisciplinary view suggests that instructing the conflicted individual to resist the interfering interest is a false solution to a conflict situation. The person's judgment risks being compromised even if she genuinely attempts to disregard the interfering factor.

IV. The Relevance of the Interdisciplinary Theory of Conflict of Interest to the Law of Fiduciary Duties

Transposed into fiduciary law theory, the interdisciplinary view advances the current understanding of the content and purpose of fiduciary duties in several respects. First, it provides a more cogent explanation of the content of fiduciary duties. Second, the theory advances the debate on the purpose of the strict proscriptive duties, by emphasizing the core fiduciary duty to exercise proper judgment. Third, the theory provides solid arguments against the calls for relaxing fiduciary duties in commercial contexts, due to the proscriptive rules' vital role in protecting the core judgment duty. Finally, the new theory shows why efforts to prevent the temptation to act self-interestedly are misplaced. The interdisciplinary view convincingly argues that the focus should be placed instead on developing strategies to manage actual or potential conflicts.

A. The Duty to Exercise Discretion Based on Relevant Considerations

The interdisciplinary view advances the current understanding of the content of fiduciary duties by emphasizing that at the core of the fiduciary's role lies the duty to exercise judgment properly. As explained in Part I, the prevailing, narrow view of the content and justification of fiduciary duties fails to connect the strict proscriptive duties with the core element of fiduciary authority. When incorporated into the fiduciary law theory, the interdisciplinary view addresses this problem, by showing the intimate link between extraneous interests and the exercise of judgment, and the various ways in which the latter can be breached. The proscrip-

tive rules protect the core fiduciary duty to identify and assess relevant considerations in the decision-making process.

It is well established that a fiduciary is bound to exercise discretion within the objective limits of her powers and in what she believes to be the best interest of the beneficiary or the purpose for which the power was granted.¹²⁸ It is also common knowledge that an appropriate exercise of discretion imposes on fiduciaries two requirements. First, a fiduciary must exercise active discretion, in the sense of applying her mind and reaching a conscious decision regarding the need for, and the implications of, exercising any power or discretion that she holds in fiduciary capacity.¹²⁹ Second, if a fiduciary decides that it is opportune to exercise a power, she must decide where the best interests of the beneficiary lie (in the case of an administrative power), or what is the best way to achieve the purpose for which the power was given (in the case of a dispositive power). The two aspects of the exercise of judgment involve a similar decision-making process: fiduciaries must decide based on relevant considerations.¹³⁰ Although this proper judgment duty is habitually discussed in trust law contexts, it applies to any person in a fiduciary position.¹³¹

The proper judgment duty has a procedural nature. It tells a fiduciary what to do when exercising discretion, rather than what is a relevant consideration for each decision.¹³² Relevant considerations to be taken into account in a particular exercise of discretion include factors such as the nature and the purpose of the particular power to be exercised, the relationship between this power and the other powers and duties of the fiduciary, or the nature of the transaction which the fiduciary intends to perform.¹³³ Furthermore, fiduciaries must have regard to the already recognized relevant factors such as “[t]he wishes, circumstances and needs of beneficiaries,” or “fiscal considerations”.¹³⁴ The weight that each of the relevant factors should carry in determining the course of action is a pure-

¹²⁸ See generally Smith, “Understanding the Power”, *supra* note 31.

¹²⁹ See Thomas, *supra* note 20 at 506.

¹³⁰ See *ibid* at 539, 555.

¹³¹ See McGhee, *supra* note 25 at para 11-009.

¹³² See Thomas, *supra* note 20 at 519–20; McGhee, *supra* note 25 at para 10-033.

¹³³ See Finn, *Fiduciary Obligations*, *supra* note 28 at 15–16.

¹³⁴ *Pitt v Holt*, [2011] EWCA Civ 197 at paras 114–16, [2012] Ch 132 [*Pitt* CA]. The UK Supreme Court upheld this decision as regards the matter of actions by trustees within the limits of their powers (see *Pitt v Holt*, [2013] UKSC 26 at para 93, [2013] 2 AC 108). In discussing the duty to take into account relevant considerations, the Court of Appeal revised what had, until then, been known as the rule in *Re Hastings-Bass* (see *Re Hastings-Bass (Decd)*, [1974] EWCA Civ 13, [1975] 1 Ch 25 at 41, [1974] 2 WLR 904).

ly subjective matter.¹³⁵ As long as fiduciaries apply their mind to the importance of a relevant consideration for a particular decision, they comply with the duty of real and genuine consideration of relevant factors, irrespective of the actual outcome of their decision.¹³⁶

The current fiduciary law lacks an in-depth insight into the multiple ways in which the proper judgment duty is at risk of being breached. Clearly, a blatant procedural flaw exists when fiduciaries exercise their powers without any exercise of judgment,¹³⁷ or when they base their decision not to exercise a power on a clearly irrelevant consideration.¹³⁸ A more insidious risk of breach, however, is largely ignored by the fiduciary law literature: the negative effect that the presence of an interfering personal interest or duty has on the reliability of judgment. The interdisciplinary view on conflicts of interest shows that, when a decision maker has an actual or potential interest in the outcome of her decision, her ability to evaluate the relevant considerations is impaired in ways that cannot be measured or corrected appropriately. The effect that the extraneous interest has on the decision-making process cannot be measured due to the nature of discretion. The existence of decision-making authority means that the exercise of judgment cannot be evaluated based on results. As the interdisciplinary view emphasizes, when discretion exists, people may disagree on the best course of action or objective to be pursued, without anyone being objectively wrong.

Applied to fiduciary law theory, the interdisciplinary view sheds light on the subtle connection between the proscriptive duties and the duty to exercise proper judgement. This connection shows why the purpose of the proscriptive duties cannot be fully understood separately from the fiduciary decision-making process.

B. Preserving the Strictness of the Proscriptive Fiduciary Duties

The prevailing misunderstanding of the notion of conflict of interest has led an increasing number of courts and commentators to call into question the necessity of maintaining the strictness of the proscriptive duties in modern legal systems. Jay Shepherd, one of the earliest authors of a general theory of fiduciary duties, argues that the no-conflict rule is mistaken. In his view, the mere fact of the fiduciary being in a situation in which she is faced with the choice of using her powers to advance her own

¹³⁵ See *Edge v Pensions Ombudsman* (1999), [2000] Ch 602 at 626 (CA), [2000] 3 WLR 79.

¹³⁶ See *Pitt CA*, *supra* note 134 at para 127.

¹³⁷ See e.g. *Turner v Turner* (1983), [1984] 1 Ch 100 at 109–10, [1983] 2 All ER 745.

¹³⁸ See e.g. *Klug v Klug*, [1918] 2 Ch 67 at 71, 118 LT 696. This case can also be considered as involving an exercise of discretion for an improper motive or purpose.

interest as opposed to the interest of the beneficiary is not reprehensible. It is only when the fiduciary chooses to use the power in her interest, and therefore the conflict is resolved and ceases to exist, that the fiduciary's liability arises.¹³⁹ Consequently, in Shepherd's view, the strict no-conflict rule is mistaken because it includes a prohibition of potential conflicts of interest.¹⁴⁰

John Langbein provides a different argument for relaxing the proscriptive duties for trust law in the United States. He claims that the "no further inquiry" rule, according to which "transactions involving trust property entered into by a trustee for the trustee's own personal account [are] voidable without further proof,"¹⁴¹ is archaic, and must be modified.¹⁴² Langbein argues that neither the evidentiary difficulties nor the deterrence themes justify the maintenance of the no-further-inquiry rule, due to the significant modernization of civil procedure and the comprehensive requirements regarding the appropriate recordkeeping by trustees. The strict prohibitions cause over-deterrence by preventing trustees from engaging in transactions that could benefit both the beneficiary and the trustee.¹⁴³ Consequently, he argues, the no-further-inquiry rule should be replaced with a regime that allows trustees to retain profits obtained from their position, as long as they can prove, if challenged in court, that the conflicted transaction was prudently undertaken in the beneficiary's best interest.¹⁴⁴

The idea of relaxing the proscriptive rules found support not only from academic commentators, but also from judges. In *Murad v. Al-Saraj*, for instance, the judges of the English Court of Appeal affirmed in obiter that the time may be ripe for the English courts to relax the traditional strict standard of liability imposed by the no-profit rule.¹⁴⁵ Lady Justice Arden observed that the traditional rationale for the irrelevance of the fiduciary's honesty in obtaining an unauthorized profit, namely the need

¹³⁹ See Shepherd, *supra* note 23 at 148–49. Shepherd accepts that, in certain exceptional cases, the strict no-conflict rule should be maintained, in the sense that the fiduciary should not be allowed to be in a position where she could decide against the beneficiary's interests (*ibid* at 342–45).

¹⁴⁰ See *ibid* at 149, where Shepherd states: "When we say 'a fiduciary may not put himself in a position where his interest and his duty conflict', we are completely wrong. Of course he can have a conflict of interest, whether passive or active. What he cannot do is choose in favour of his interest."

¹⁴¹ Langbein, *supra* note 87 at 931, citing Uniform Trust Code § 802 cmt (2000).

¹⁴² See Langbein, *supra* note 87 at 947.

¹⁴³ See *ibid* at 951–57.

¹⁴⁴ See *ibid* at 980–81.

¹⁴⁵ See *Murad*, *supra* note 3 at 82–83, 121.

for deterrence combined with evidentiary difficulties, is obsolete and can no longer justify the stringency of the rule. A satisfactory degree of deterrence can be achieved by putting on fiduciaries the burden to prove that they acted in good faith and for the benefit of the beneficiaries. Furthermore, the flexibility of the contemporary civil procedure rules will adequately protect the principal, and strike the right balance between the interests of the parties.¹⁴⁶ Charles Mitchell agrees with Lady Justice Arden's view that the no-profit rule should be relaxed in order to prevent excessively harsh outcomes for fiduciaries. In his view, the courts should have the power to alter the severity of the rule artificially, either by narrowing the scope of the fiduciary's undertaking, so that the fiduciary's gains would fall outside the scope of her duty, or by readjusting the requirement of remoteness by "deem[ing] the gains to be too remote a consequence of the breach to justify ordering the fiduciary to turn them over."¹⁴⁷

At first sight, it is tempting to agree that the inflexible no-conflict and no-profit rules are anachronistic and therefore should be adapted to new commercial realities. Based solely on the traditional explanations for the strictness of the proscriptive duties (namely, deterrence and evidentiary difficulties), one may be tempted to agree that punishing a fiduciary who obtained a gain while acting in good faith in the interests of the beneficiary is unjustifiably harsh. The relaxation arguments provided by judges and commentators, however, are premised on a superficial understanding of the notion of conflict of interest and of the main role that the proscriptive duties serve.

The proper understanding of the notion of conflict of interest brought by the interdisciplinary view reveals that there is a more profound reason why no actual or potential conflict of interest should be allowed: the mere possibility of a conflict, even if does not arise at the beneficiary's expense, affects the way in which the fiduciary exercises professional judgment over the beneficiary's interests.

C. Addressing Conflicts of Interest: The Shortcomings of Resistance and Disclosure

Applied to the context of fiduciary law theory, the interdisciplinary view of conflicts of interest is also helpful in refining the current understanding of what constitutes an effective response to conflict situations. While the interdisciplinary view does not prescribe a single optimal re-

¹⁴⁶ See *ibid* at paras 82–83.

¹⁴⁷ Charles Mitchell, "Causation, Remoteness, and Fiduciary Gains" (2006) 17:2 KCLJ 325 at 339.

sponse to a conflict situation, it sheds light on the shortcomings of two of the most frequently invoked responses: resisting the temptation of self-interest and disclosing the conflict.

Resisting self-interest is not an adequate solution to a conflict situation because decision makers have an imperfect understanding of the effect of self-interest on their judgment and of the optimal way of correcting the biases that self-interest creates.¹⁴⁸ One line of research shows that decision makers tend to underestimate the biasing effect of self-interest on themselves. They tend to discount self-interest in assessing their own motivation and to overestimate the role that self-interest plays in motivating other people.¹⁴⁹ Other studies show the opposite tendency. When decision makers are aware of a situation where a self-interest bias could plausibly exist, they tend to assume that the bias exists and that it is influencing their decision-making processes. The more committed a decision maker is to fairness and objectivity, the more likely she is to overcompensate for the presumed bias of self-interest, thereby undermining the quality of her decision. This “incorrect correction” is caused by the decision makers’ inability to gauge the actual effect of self-interest on her own judgment.¹⁵⁰

Disclosure and consent also have shortcomings that are yet to be fully recognized in fiduciary law theory. It is generally accepted that complete disclosure will give the beneficiaries the opportunity to give informed consent to the situation of conflict, to adjust reliance accordingly, or to replace the fiduciary.¹⁵¹ When the fiduciary is not replaced, disclosure is an effective response only if it does not affect the fiduciary’s judgment process, or alternatively, if the beneficiary is “able to correct [adequately] for [a] biasing influence.”¹⁵² Yet, psychological research shows that neither of

¹⁴⁸ See generally Timothy D Wilson, David B Centerbar & Nancy Brekke, “Mental Contamination and the Debiasing Problem” in Thomas Gilovich, Dale Griffin & Daniel Kahneman, eds, *Heuristics and Biases: The Psychology of Intuitive Judgment* (Cambridge: Cambridge University Press, 2002) 185; Richard E Nisbett & Timothy DeCamp Wilson, “Telling More Than We Can Know: Verbal Reports on Mental Processes” (1977) 84:3 *Psychological Rev* 231.

¹⁴⁹ See Emily Pronin, “Perception and Misperception of Bias in Human Judgment” (2007) 11:1 *Trends in Cognitive Sciences* 37 at 37–38.

¹⁵⁰ See Wilson, Centerbar & Brekke, *supra* note 148 at 191–92; Amy D Shelton, “Incorrect Correction for the Self-Interest Bias: How Naïve Theories of Bias Can Contribute to Poor Decision-Making” (BA Thesis, Williams College, 2005) at 7–8 [unpublished].

¹⁵¹ See Matthew Conaglen, “The Extent of Fiduciary Accounting and the Importance of Authorisation Mechanisms” (2011) 70:3 *Cambridge LJ* 548 at 563–64.

¹⁵² Daylian M Cain, George Loewenstein & Don A Moore, “The Dirt on Coming Clean: Perverse Effects of Disclosing Conflicts of Interest” (2005) 34:1 *J Leg Stud* 1 at 3 [Cain, Loewenstein & Moore, “Perverse Effects”].

these conditions may be met. Sometimes both parties may be worse off following disclosure.¹⁵³

Disclosure may have the unintended consequence of liberating a fiduciary from concerns about ethicality and giving her a moral licence to incorporate the conflicting interest into the decision-making process.¹⁵⁴ Knowing that the beneficiary is likely to discount the decision to correct for the self-interest, the fiduciary may be tempted to counteract this adjustment by allowing self-interest to influence her own decision even further.¹⁵⁵ Yet, there is also evidence showing that beneficiaries of disclosure do not adjust to counteract the self-interest. Paradoxically, beneficiaries could then see disclosure as a sign of the fiduciary's trustworthiness, and may increase their confidence in the latter's judgment.¹⁵⁶ Moreover, beneficiaries of disclosure are unlikely to be sophisticated enough to be able to adequately adjust their reliance on the conflicted fiduciary.¹⁵⁷

Understanding the shortcomings of resistance and disclosure is an essential first step toward designing more effective responses to a conflict situation. The current emphasis that fiduciary law scholarship places on resisting the temptation of self-interest and on disciplining the fiduciary market should be replaced with a focus on recognizing and managing conflicts of interest. Moreover, an adequate awareness of the potential unintended effects of disclosure and consent is essential when the parties to a fiduciary relationship consider how to respond to a conflict situation.

Conclusion

The proper exercise of judgment or discretion is the main objective of the law in regulating fiduciary relationships. Irrespective of the label used (fiduciary duty, duty of loyalty, duty to exercise sound discretion, or duty of real and genuine consideration), the central duty binding every person holding a fiduciary power aims at guiding the fiduciary's exercise of discretion by controlling the decision-making process.

¹⁵³ See Daylian M Cain, George Loewenstein & Don A Moore, "Coming Clean but Playing Dirtier: The Shortcomings of Disclosure as a Solution to Conflicts of Interest" in Don A Moore et al, eds, *Conflicts of Interest: Challenges and Solutions in Business, Law, Medicine, and Public Policy* (Cambridge: Cambridge University Press, 2005) 104 [Cain, Loewenstein & Moore, "Shortcomings of Disclosure"].

¹⁵⁴ See Cain, Loewenstein & Moore, "Perverse Effects", *supra* note 152 at 7.

¹⁵⁵ See Cain, Loewenstein & Moore, "Shortcomings of Disclosure", *supra* note 153.

¹⁵⁶ See Cain, Loewenstein & Moore, "Perverse Effects", *supra* note 152 at 5–6.

¹⁵⁷ See *ibid* at 20–21.

The centrality of the decision-making process explains why fiduciary law comprises stringent proscriptive duties. Any decision made in a conflict of interest situation undermines the integrity of the decision-making process, irrespective of the actual outcome of the decision. Although the biasing effect of self-interest on judgment is well established in cognitive and behavioural research, contemporary fiduciary law theory largely ignores its existence.

One of the main causes of this oversight is the continuous attempt to find a theoretical foundation for the proscriptive duties independently of the essential feature that is specific to a fiduciary position. The view that has dominated fiduciary law theory is based on the premise that fiduciaries inevitably exploit their superior position, and therefore need to be disciplined. The law's objective of preventing abuse or misappropriation, however, spreads across various legal doctrines and areas. Therefore, it cannot be the central feature that sets fiduciary law apart. The essence of the fiduciary principle is the authority to decide how to advance the best interest of another or to promote certain abstract purposes. A fiduciary must not exercise this authority capriciously. She must identify and evaluate the considerations that are relevant to each exercise of discretion. Recent cognitive and behavioural research concerned with conflicts of interest shows that self-interest can affect the decision maker's ability to evaluate these relevant considerations in ways that often escape measurement or control. The main reason why fiduciary law is concerned with the management of actual or potential situations of conflict is not to prevent abuse by stifling self-interest. Rather, it is to protect the beneficiary's right to the fiduciary's unencumbered and genuine judgment. Disciplining legal actors and reinforcing the general confidence in legal relationships are, at best, secondary effects of fiduciary law and, indeed, of any private law rules.
