

## DISCLOSURE OF A DIRECTOR'S INTEREST IN A RIVAL COMPANY

*Shanghai Hall Ltd. v. Chong Mun Foo*<sup>1</sup>

In *Shanghai Hall Ltd. v. Chong Mun Foo*, the defendants were the directors of the plaintiff company which operated a restaurant and bar. The defendants, without the knowledge of the other members of the company, were also the directors of a rival company which had its place of business one floor below that of the plaintiffs. The first defendant, who was the managing director of the plaintiff company, induced twenty-five of its employees to resign and to join the rival company instead. On subsequent discovery of the facts the plaintiff company brought an action against the defendants alleging breach of their duties as directors towards the plaintiff company by not disclosing the nature of their interests in the rival company.

The case came before the Court as an application by the defendants to strike out the plaintiffs' statement of claim. The judge stated that "the only question to be determined here is whether a director of a company is prohibited from becoming a director of a rival company."<sup>2</sup> He cited the case of *London and Mashonaland and Exploration Co. Ltd. v. New Mashonaland Exploration Co. Ltd.*<sup>4</sup> as being the case in point. This case, according to the judge, decided that in the absence of a prohibition appearing in the regulations of a company, a director is at liberty to become a director of a rival company. The learned judge then considered Art. 94 of the articles of association of the plaintiff company. This article dealt with the question of disclosure when a director has an interest in another company which is about to make certain contracts or arrangements with the company. The judge then on the authority of the *Mashonaland* case<sup>4</sup> concluded that since the articles of association in question did not prohibit a director from becoming a director of a rival company, the issue would be decided against the plaintiffs.

But on reading the judgment one is not certain whether the real issue was actually decided. The learned judge said:

The plaintiffs now alleged that defendants had not disclosed the nature of their interests in the rival company and they accordingly contend that the defendants were by their conduct fraudulent and constituted a breach of a director's duty towards the plaintiffs.<sup>3</sup>

From the facts, it would certainly be to the plaintiffs' advantage to treat this as the issue and not what the learned judge stated to be the issue. For the plaintiffs to have alleged that the defendants had not disclosed the nature of their interests in the rival company, it must by implication have been accepted by the plaintiffs that the defendants had the right to join the rival company. What they were complaining about was that the duty of disclosure, concomitant with such a right, was not discharged by the defendants. Therefore it would be highly improbable that the plaintiffs would wish to treat the issue to be whether a director can also be a director of a rival company.

Suppose the learned judge had taken as the issue that alleged by the plaintiffs, that is, a director who has an interest in a rival company must disclose the nature of his interest to his fellow directors, would the plaintiffs have succeeded then? It is submitted that they would still not. Their action was brought before the Malaysian Companies Act, 1965,<sup>6</sup> came into force, and therefore had to be decided under the law prior to the Act. But the then governing legislation, the Malayan Union Companies Ordinance, 1946,<sup>7</sup> was silent on the point as to whether a director has such a duty of disclosure. Nor is there any case authority which indicates that

1. [1967] 1 M.L.J. 254.

2. *Ibid.*, at p. 265.

3. [1891] W.N. 165.

4. *Ibid.*

5. *Ibid.*, at p. 255.

6. No. 79 of 1965.

7. No. 13 of 1946.

such a duty exists at common law. This being so, the plaintiffs' allegation in the instant case would still have failed as there would have been neither statutory provision nor precedent to exact from the defendants the particular duty.

However, if a similar issue should arise under the 1965 Act, it will be governed by subsections (5) to (8) of section 131 thereof. This section, like most of the other sections of the Act, is Australian in origin. S. 131(5) reads:

Every director of a company who holds any office or possesses any property whereby whether directly or indirectly duties or interests might be created in conflict with his duties or interests as director shall declare at a meeting of the directors of the company the fact and the nature character and extent of the conflict.

The effect of this subsection is very wide. It would probably extend further than the mere question of whether a director need disclose that he holds property or office(s) in a rival enterprise. It would appear to cover any case where a director holds other office which might place him in a position where interest and duty conflict.

It might be noted that not only must a director in cases of conflict disclose the "fact" of the conflict, that is, to announce to his fellow directors at the "first meeting"<sup>8</sup> that he is holding such an office, but he must also declare the "nature character and extent of the conflict." This may mean that the director must explain the powers and duties of such office and how in exercising these powers he "might" come into conflict with the company ("nature character . . .")<sup>9</sup> and how far he anticipates the scope of the conflict would be ("extent"). Difficulty may arise as to what degree of foresight must the director have in predicting the "extent" of the conflict; and as to the standard by which he is to be judged liable if he fell short of the foresight expected.

8. S. 181 (6) — “The declaration shall be made at the first meeting of the directors held —
  - (a) after he becomes a director, or
  - (b) (if already a director) after he commenced to hold the office or to possess the property — as the case requires.”

9. There seems to be little difference between “nature” and “character”.