THE FIDUCIARY DUTIES OF COMPANY DIRECTORS

by

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(ZURA BTE YAHYA)

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PREFACE

As our business world is getting more developed and complex, Legislatures have developed legislations to regulate and control the companies which are being incorporated. This can be seen in several countries such as Malaysia, Singapore, Australia, Great Britain and Ghana. In the Companies Acts of these countries, there are provisions on the director's duties. This is because the role of a company director is critical in the effective and efficient operation of the company. However not all aspects of the director's duties are codified. This project paper attempts not only at pointing out the director's duties which have received statutory recognition but also other duties which arise from conflict of duties and interests. As will be seen from the discussion in this paper, a company director is a fiduciary. Therefore he cannot occupy a position where his duties and interests conflict. Any profits which are obtained from this conflict must be disgorged. However at present it is still arguable whether the rule against non-profiteering should be strictly adhered to or not.

This paper also attempts to analyse the various fiduciary duties of a director. The aim is to show the importance of the equitable principles for the purpose of regulating the conducts of the director in managing the affairs of the company. It is hoped that fiduciary duties of directors should not be disregarded just because of the

availability of the statutory provisions. The enforcement of the equitable rules will ensure that the director will not obtain secret profits from the company.

Lastly, I will like to express my gratitude to my supervisor, Encik Shaukat Ali, for his kind and patient guidance in the preparation of this project paper.

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INTRODUCTION

In this project paper, an examination is made in regard to the long established equitable principle that a person in a fiduciary position must not occupy a position in which there will be a conflict of duties and interests. If the person does occupy such a position he will be in breach of his fiduciary duty. As a result action can be taken against him, and one would be entitled to be awarded with one of the several remedies available. However the scope of the above-mentioned principle is limited to the position occupied by the company directors. Thus the purpose of this project paper precisely is to see the consequence of the above equitable principle in regard to the company directors.

Since the above equitable principle is applicable to persons in fiduciary position, thus in Chapter I, discussion is centred around the issue whether the director is in a fiduciary relationship with the company. So an historical development of the word 'fiduciary' is being traced. From the examination of decided cases, it has become certain that directors, though they may be called trustees or agents of the companies, are indeed in fiduciary relations with their company. Since directors are fiduciaries, so in Chapter II, the question whether the equitable principle should be strictly adhered to or not is discussed.

The consequences which ensue concerning the fiduciary duties of directors when they place themselves in a position of a conflict of

interest and duty are dealt with from Chapter III to Chapter VII. The fiduciary duties which are involved are those in regard to confidential information, corporate opportunities, competing interests, contracts with the company, and also the dealings with the company's properties. In all these five chapters, besides examining these duties as provided by equity, references are also made to statutory provisions concerning these duties.

Chapter VIII deals with the defence in which the directors can put forward when they act in breach of any of their fiduciary duties. This chapter also provides for remedies in which one is entitled to ask in court when the directors are in breach of their fiduciary duties.

In this project paper the rigidity of the equitable principle of conflict of duty and interest in regard to the company directors will be exposed. This can be seen in all the chapters dealing with the directors' fiduciary duties. In all these chapters too, the adverse effect which the company would face when this principle is strictly adhered to, are also pointed out. Thus with this project paper it is hoped that the court will reconsider its attitudes concerning the fiduciary duties of the directors. This equitable principle should not be strictly adhered to at the expense of the efficiency and the smooth functioning of the company in particular and the commercial world in general.

CHAPTER I

ORIGIN AND DEVELOPMENT OF THE TERM "FIDUCIARY"

A lot of discussion has ensued as to the position which are occupied by the company directors. From these discussions two schools of thought have evolved. One school of thought regards them as being the trustees for the company. The other school says that directors are agents for the company. But whether the directors are trustees or agents, they are in fiduciary relationship with their company. The existence of the fiduciary relationship between the directors and their company was established in Regal (Hastings) Ltd. v. Gulliver.[1]

Before going any further into the various fiduciary duties of the company director, a knowledge of the development of this fiduciary concept would be of a great help. The development of this concept is going to be traced according to the following headings:-

(A) Background and development of the concept.

(B) Its position in the Modern Law.

(C) Its extension to the post of the company director.

(A) Background and development of the concept

The term "fiduciary" is a recent terminology. In the eighteenth and nineteenth centuries the phrase "fiduciary relationship" was not used. Instead such a relationship was described as one in which the

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[1] [1967] 2 A.C. 134.

persons were in the position of trust or confidence. Thus in many matters of confidence, they were called "trusts" regardless of whether there were any strict trusts of property or not. This could be seen in Charitable Corporation v. Sutton.[2] In this case Lord Hardwiche said that the board of "committee-men of the corporations were most properly agents to those who employ them in this trust". Another case in which this matter can be observed is Duke of Beaufort v. Berty.[3] Here the chancellor was asked to interfere in the choice of schools which had been made by the infant's guardians. During the proceeding, it was reported that the chancellor had interrupted the counsel to say that the guardians were trustees. In his judgement he said that:-

> ".... as the court would interpose where the estate of a man was devised in trust, so would it a fortiori concern itself on the custody of a child being devised to a guardian, who was but a person entrusted in that case... That if any wrong had been done .... the court would interpose and order the contrary; and that this was grounded upon the general power and jurisdiction which it had over all trusts, and guardianship was most plainly a trust."

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[2](1742) 2Atk. 400.

[3](1721) 1P. Wms 70.

From the two cases mentioned above, it can be said that during that period when relationship of confidence existed between the parties, they were in trust position. The acceptability of the position of trust was recognised in Gartside v. Insherwood.[4] In this case the principle laid down was that "if a confidence is reposed and that confidence is abused, a court of equity shall give relief." This clearly shows the words "confidence" and "trust" are the only terms used during that time to describe the present fiduciary relationship.

At times however, discretion based on broad principles gave way to concrete rules with a standard technical vocabulary. Descriptive words like "trust" and "confidence" which once dominated this field gave way to precise terms which were better suited to the formulation of fixed rules. The word "trust" comes to be recognised as a formal term with its modern technical meaning. This means situations which were formerly described vaguely as "trusts" were now left without a name. This had resulted in uncertainty. The uncertainty could be seen in several reported cases of the early nineteenth century. For instance in York Buildings Co. v. Mackenzie[5], the counsel was obviously put to pain to express himself when he pleaded for the application of the traditional principles. His pleading is as follows:-

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[4](1788) 1 Bro. C.C. 558.

[5](1795) 8 Bro. PC 42 at p. 64.