

In the Privy Council

No. 51 of 1982

ON APPEAL FROM THE SUPREME COURT OF HONG KONG

(APPELLATE JURISDICTION)
CIVIL APPEAL NO. 64 OF 1982

(On appeal from High Court Commercial List No. 19 of 1982)

SAMUEL TAK LEE	BETWEEN	
	and	Appellant
CHOU WEN HSIEN		1st Respondent
CHOW CHUNG KAI		2nd Respondent
ANN TSE KAI		3rd Respondent
GAW SIONG CHWAN		4th Respondent
HSIN TING CHIA		5th Respondent
HU CA FEE		6th Respondent
CHENG WEI SHUE		7th Respondent
OCEAN LAND DEVELOPMENT LIMITED		8th Respondent

CASE FOR THE RESPONDENTS

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CASE FOR THE RESPONDENTS

1. This is an appeal from a judgment of the Court of Appeal of Hong Kong (Cons and Zimmern, JJ.A and Hooper, J.) dated the 9th day of July, 1982, dismissing with costs the Appellant's appeal from an order of Fuad, J. in chambers in the High Court of Hong Kong dated the 20th day of May, 1982 whereby it was ordered that
- 10 (i) the general endorsement of the Writ of Summons dated the 15th day of May 1983 be struck out and the action be dismissed with costs payable to the Respondents by the Appellant;
- (ii) the interlocutory injunctions granted by the Honourable The Chief Justice on the 15th day of May, 1982 be discharged; and
- (iii) Certificate for two counsel.
2. The judgment of Fuad, J. giving his reasons for making the said Order was delivered on the 24th day of May, 1982.
3. The questions for decision on this appeal involve the construction of Article 73(d) of the Articles of Association of the 8th Respondent. Article 73 provided as follows:—
- 20 "73. The office of an Ordinary Director shall be vacated:—
- (a) If he becomes bankrupt or insolvent or compounds with his creditors;
- (b) If he becomes of unsound mind;
- (c) If he be convicted of an indictable offence;
- (d) If he is requested in writing by all his co-directors to resign;
- (e) If he becomes prohibited from being a Director by reason of any order made under Section 223 or 275 of the Ordinance;
- (f) If he gives the Company one month's notice in writing that he resigns his office.
- 30 But any act done in good faith by a Director whose office is vacated as aforesaid shall be valid unless, prior to the doing of such act, written notice shall have been served upon the Company or an entry shall have been made in the Director's Minute Book stating that such Director has ceased to be a Director of the Company."
4. By a notice in writing signed by the 1st to 7th Respondents, bearing date the 12th day of May 1983, addressed to the Appellant and delivered to him on the 15th day of May 1982, the Appellant was requested to resign his office as a director of the 8th Respondent pursuant to Article 73(d) of the Articles of Association of the 8th Respondent. The 1st to 7th Respondents and the Appellants were, immediately prior to the delivery of the said notice, the only directors of the 8th Respondent.

Record
p.135, L.1
— p.143 L.3

p.21 L.1-14

p.1 L.1 —
p.4 L.10

p.21 L.15 —
p.26 L.20

p.38 L.9 &
L.13
p.38 L.9 —
L.21

p.101 L.17 —
p.102 L.8

5. The points raised in this appeal are:—

- (i) Whether the office of director is automatically vacated on the giving of such a request pursuant to Article 73 (d);
- (ii) Whether such request can in any circumstances be set aside if it is established that the directors signing the same, or any of them, were in so doing acting in breach of their duty to the 8th Respondent, namely failing to act bona fide in what they considered to be the best interests of the 8th Respondent;
- (iii) If it is decided that the question whether any of the directors signing the request acted in breach of his said duty in so signing is in any circumstances relevant:—
 - (a) whether such a breach would make the request void or voidable;
 - (b) if the latter, whether voidable only at the instance of the 8th Respondent;
- (iv) Whether the Appellant would be entitled to bring these proceedings in his personal capacity as a director even if it was established that all or any of the directors signing the request did so in breach of their said duty;
- (v) Whether the Writ of Summons ought to have been struck out and the action dismissed before the trial of the action.

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6. The 8th Respondent is a public quoted company incorporated in Hong Kong on the 11th day of August, 1972. At all material times, the 1st Respondent has been the chairman of the board of directors of the 8th Respondent.

7. The 2nd to 7th Respondents have at all material times been directors of the 8th Respondent, as was the Appellant until his office of director was vacated pursuant to the said request under Article 73(d).

8. In the early evening of Saturday, the 15th day of May, 1982, the Appellant made application ex. parte to the Chief Justice of Hong Kong at his residence for various orders against the Respondents. The Chief Justice made orders which were designed to restore the Appellant to his office as a director of the 8th Respondent. The Writ of Summons was also issued on the 15th May, 1982. The avowed basis of the application as disclosed by the Appellant's affidavit of the 15th day of May, 1982 is breach of the said duty by the 1st to 7th Respondents. It has throughout been plain from the form of the proceedings and the manner in which the same were conducted:—

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p.1 L.1-40 to
p.4 L.1-10

p.4 L.11-
p.5 L.34

p.19 L.20-
p.20 L.30

p.1 L.1-
p.4 L.10

p.9 L.21-
p.13 L.8

- (a) that the Appellant's proceedings were brought by him in the capacity only of director, that he was not suing as shareholder and, in particular, not as representative of other shareholders on behalf of the 8th Respondent;
- (b) that the Appellant did not deny that the said request was a request in writing to resign signed by all his co-directors and duly given to him pursuant to the said Article 73(d).

10 9. The order made by the Chief Justice was served on some of the Respondents on the 17th May, 1982, and in the time available before the return date, the only evidence in reply was the affirmation of the 6th Respondent made on the 18th day of May, 1982 and in particular paragraphs 4 to 6 thereof denying the allegation that the request was not made in the best interest of the 8th Respondent.

p.130 L.21-
p.131 L.26
p.131 L.1-20

20 10. The return date for the order made by the Chief Justice was at 10 a.m. on the 19th day of May, 1982 before Fuad, J. On this hearing, and in the Court of Appeal of Hong Kong, the 1st and 2nd Respondents were separately represented from the other Respondents, and both sets of Respondents took out summonses to strike out the Appellant's Writ of Summons and for the action to be dismissed. Both these summonses were made returnable before Fuad, J. on the 19th day of May 1982, and the grounds of the application therein stated were as follows:—

p.8

p.8 L.5-8
p.8 L.29-32

- (1) the action is irregularly constituted;
- (2) the Writ discloses no reasonable cause of action;
- (3) the action is frivolous, vexatious and is otherwise an abuse of the process of this Honourable Court.

30 11. Fuad, J. decided to hear the said Summonses issued by the Respondents first, and accordingly the Respondents did not seek an adjournment in order to supplement their evidence. Upon the conclusion of argument on the Summonses, Fuad, J. struck out the Writ of Summons, dismissed the action, and discharged the orders made by the Chief Justice on the ground that, since the request complied with the provisions of Article 73(d), the article became operative, and the directors' motives in making the request cannot be investigated. His Lordship took the view that the Writ of Summons was, in the circumstances, frivolous and vexatious.

p.25 L.20-26

p.26 L.8-9

12. Fuad, J. did not expressly base his reasons on the other grounds of the Summonses to strike out.

p.8 L.28-29
L.7-8

p.132 L.13 —
p.133 L.30

13. By Notice of Appeal dated the 26th day of May, 1982, the Appellant appealed to the Court of Appeal of Hong Kong on the grounds that Fuad, J. erred in pronouncing the request valid in law despite the allegations of breach of duty and that Fuad, J. did not have any material before him to conclude that the Appellant's case was plainly and obviously bad.

p.134 L.1-29

14. By a Respondent's Notice dated the 5th day of June, 1982, the Respondents repeated their contention that the action was improperly constituted and that the Appellant had no locus standi to sue in his own name.

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15. The Appellant's appeal to the Court of Appeal of Hong Kong came on for hearing on the 22nd day of June, 1982 and lasted approximately three days. The arguments for the Appellant were summarised in the judgment of Cons, J.A. The crux of the argument was that the 1st to 7th Respondents' request to the Appellant pursuant to Article 73(d) was of no effect since it was made in breach of their said duty to the 8th Respondent.

p.143 L.1-5

16. In the Court of Appeal, Cons, J.A. with whose judgment Hooper, J. agreed, said of the main argument:—

p.137 L.3-8

“With respect to counsel it seems to me impossible to maintain that the request has not taken effect. The language of the article leaves no room for doubt or uncertainty. The office shall be vacated once any event therein mentioned occurs. That vacation must take place immediately. The position would otherwise be intolerable. No one would know who really constituted the board.”

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p.137 L.9-20
p.23 L.19-23

17. In coming to that conclusion, Cons, J.A. as Fuad, J. had done in the court below, was following the decision of Farwell, J. in **In re Bodega Company Limited**, [1904] 1 Ch. 276 where the relevant article provided as follows:—

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p.137 L.10-13

“The office of any director shall be vacated — if he becomes bankrupt, if he becomes lunatic..... if he be concerned in or participate in the profits of any contract with the company not disclosed to and authorised by the board.”

18. In that case the last mentioned event had taken place. Farwell, J. at p.283 of the judgment said this:—

“In my opinion it is quite plain on the words of the article that he ipso facto, or automatically, vacates his office on the act being done; there is no distinction between this and the

other events mentioned in the article, e.g. bankruptcy, and in none of them is there any locus poenitentiae for him, or any means by which the directors can condone the offence or the act which causes the vacation. The office is vacated automatically.’’

19. In the court below, Fuad, J. had, in effect, accepted that Article 73(d) did not involve the exercise of a power, and that all the Court had to ascertain was whether the event as mentioned in Article 73(d) had taken place. p.23 L.19-23

10 20. In the Court of Appeal, Cons, J.A. disagreed with Fuad, J. on this point, and held that in requesting the Appellant to vacate his office of director of the 8th Respondent, the 1st to 7th Respondents acted as directors and were exercising fiduciary powers. p.138 L.36-37

21. Zimmern, J.A., while agreeing with Cons, J.A. that under Article 73(d) the 1st to 7th Respondents as directors were vested with a power to bring about the Appellant’s vacation of office as a director of the 8th Respondent, agreed with the conclusion of Fuad, J. as follows:— p.142 L.16-19
p.142 L.19-34

20 “In my view, the promoters of the Company in so framing Article 73(d) had been careful in avoiding any suggestion that such powers are to be exercised by committee at a board meeting. There is no mention of any resolution, notice or agenda for a board meeting. All that is required in the clearest possible language is for all the co-directors to sign a request in writing and the requested director is out of office. I agree with the learned judge in the Court below that the exercise of the power under this sub-article cannot be challenged by the ousted director either personally or in a derivative action, save in instances of actual fraud. An aggrieved ousted director can have no conceivable cause of action against the Company.
30 Each director accepted appointment with full knowledge of Article 73(d) which binds him. The co-directors when exercising that power do not act collectively as a board nor do they act on behalf of the Company which in turn has no cause of action against the co-directors. I am of the opinion that the power is vested in each director personally to be exercised in that very limited way as he thinks fit without being tied by fiduciary duties to the Company. If it were otherwise there would be uncertainties about the composition of the board and this case is an example. Such uncertainties are rarely
40 in the best interests of the Company.’’

p.140 L.1-14

22. The Court of Appeal of Hong Kong, however, was unanimous in holding that the Appellant had no locus standi to bring the action. Cons, J.A. with whom both Zimmern, J.A., and Hooper, J. agreed on this point, took the view that even if a wrong had been done by one or more of the 1st to 7th Respondents signing the said request in breach of their said duty to the 8th Respondent, that wrong was done only to the 8th Respondent. As the Appellant did not choose to bring the action as a minority shareholders' action on behalf of the 8th Respondent, he had no right to sue.

p.141 L.10-11

23. Cons, J.A. rejected the view that a wrong had been done to the Appellant personally. It is respectfully submitted that this is correct. A wrong would have been done to the Appellant personally if he had been excluded from the deliberations of the Board of directors without any reliance by his co-directors on the powers of removal given by Article 73(d). Once it is accepted (as the Appellant has accepted) that the said request was given pursuant to and in accordance with the formal requirements of Article 73(d) the Appellant, whose contract as a director was on the terms that Article 73(d) applied thereto, is bound by the said request and cannot question whether any of the directors signing it was acting in breach of his duty to the 8th Respondent.

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24. An act done by the directors in breach of their duty to their company is not void. It may, subject to any supervening rights of third parties, be avoided by the company (as the person to whom the duty is owed) or (in cases where an exception to the rule in **Foss v. Harbottle** (1843) 2 Hare 461, is applicable and is relied on) in proceedings brought by shareholders on behalf of the company. The act may be ratified by a resolution of the company in general meeting. The act, unless and until avoided as aforesaid, is valid and effective for all purposes. In particular a party in a contractual relationship with the company cannot escape the consequences of an act done on behalf of the company in pursuance of that contract on the ground that the directors who did the act were in breach of their duty to the company in doing it.

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25. Accordingly if, contrary to the submissions of the Respondents, any of the 1st to 7th Respondents acted in breach of his duty to the 8th Respondent in signing the said request:—

- (a) the same nonetheless remains valid and effective for all purposes unless avoided by the 8th Respondent or by the Court in proceedings brought by a shareholder on behalf of the 8th Respondent, being proceedings which properly fall within one of the exceptions to the said rule in **Foss v. Harbottle**;
- (b) the breach of duty may be ratified by resolution passed by a general meeting of the 8th Respondent;

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- (c) the Appellant may not rely on the breach of duty in order to escape the consequences of the said request, the giving of which was an act done on behalf of the 8th Respondent in pursuance of the contract between the 8th Respondent and the Appellant as one of its directors.

10 26. These were, in substance, the submissions which found favour with the Court of Appeal of Hong Kong. The Court of Appeal found that the authorities relied on by the Appellant, in particular **Pulbrook v. Richmond Consolidated Mining Co.** (1878) 9 Ch.D. 610 and **Hayes v. Bristol Plant Hire Limited** [1957] 1 W.L.R. 499, were cases where the director was able to show that the provisions of the articles of association necessary for his vacation of office did not apply at all.

27. Cons, J.A. then considered whether it would be right to have the Appellant's action stopped in limine, and concluded that, in the light of the conclusions already reached by him and despite the elaborate arguments put before the Court of Appeal of Hong Kong the Appellant's cause of action was obviously and almost uncontestably bad: the other members of the Court of Appeal concurred. The Court of Appeal therefore dismissed the Appellant's appeal.

p.141 L.35-42

20 28. On the 30th day of July, 1982, the Court of Appeal of Hong Kong made an order granting leave to appeal to Her Majesty in Council.

p.144 L.1-20

29. The Respondents submit that this appeal should be dismissed with costs for the following amongst other

REASONS

1. **BECAUSE**, on the true construction of Article 73(d), once the request complied with its provisions, the article took effect; the event envisaged by the article to cause the vacation of the office of director has occurred, and the office of director held by the Appellant is vacated.

2. **BECAUSE**, as Fuad, J. rightly held, since the request complied with Article 73(d), the article applied, and the motives of the 1st to the 7th Respondents in making the request cannot be investigated, so that even if all or any of them were in breach of duty to the 8th Respondent, in signing the request, the request has taken effect, with the necessary consequences.

3. **BECAUSE**, as Zimmern, J.A. rightly held, even if Article 73(d) conferred a power on the 1st to 7th Respondents as directors, they do not when exercising that power act collectively as a board nor do they act on behalf of the 8th Respondent, and the exercise of the power is not tied to the fiduciary duties owed by directors to their company. 10

4. **BECAUSE**, as the Court of Appeal rightly held, the request, even if some or all of the 1st to 7th Respondents acted in breach of duty to the 8th Respondent in signing it, was not void, but only voidable at the instance of the 8th Respondent or in proceedings properly brought on its behalf. It was an act capable of ratification by the 8th Respondent in general meeting and the Court will not interfere. It was therefore a valid act under the Articles and the Appellant, who is bound thereby, cannot complain in his personal capacity 20 that a wrong has been done to him.

5. **BECAUSE**, as the Courts below have rightly held the Appellant's causes of action were plainly and obviously bad.

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BETWEEN

SAMUEL TAK LEE Appellant

and

CHOU WEN HSIEN 1st Respondent
CHOW CHUNG KAI 2nd Respondent
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