UNDERSTANDING THE LAW ON CORPORATE OPPORTUNITY: INPUTS FOR INDIA

Abstract

Balancing directorial entrepreneurialism with ensuring the director's undivided loyalty to the company is a key challenge. In a dynamic commercial context, the exacting sanctity of the director's duty to avoid situations of conflict between personal interests and company welfare has to be qualified. In India, the rules governing usage of corporate opportunity are specially relevant. However, there is little clarity on the applicable rules as Indian courts have hardly dealt with the issue. This paper presents a thorough analysis of the law on corporate opportunity and posits the framework for interpreting the no-conflict principle codified in the Companies Bill, 2012. Towards this objective, the paper scrutinizes various landmark cases and the approaches used in their reasoning such as the traditional strict English approach, a pragmatic dilution of the strict approach and the flexible US approach.

"It is not the source of the information, but the use to which it is applied, which is important in these matters"

Lindley L.J.[1]

I Introduction

THE DEVELOPMENT of the rules governing the conduct of a director when the director is faced with an opportunity/information which could benefit him individually, while acting in a corporate capacity is an area, which seemingly simple, has seen confusing jurisprudence elsewhere despite very few cases considering it in India. A balance must be struck between the nature of duty owed by the director to the company and the restriction on his capacity to use the opportunities which come his way. Manifold legal issues arise in this search for a precise balance. One must appreciate that despite this duty of not using corporate opportunity owed by the director being different from other fiduciary duties, the duties of trustees or the fiduciary duty of loyalty are instructive in defining this duty. The fiduciary framework was developed as the best approach to limit the self-interest of the management from overtaking company welfare.

This paper analyzes multiple case-law highlighting the basis for the rules governing corporate opportunity, map the arguably changing legal stances post the strict approach advocated in *Keech* v. *Sandford,*[2] and famously adopted in *Regal (Hastings)* v. *Gulliver,*[3] examine the differences in the approach of the UK courts and the US courts and finally, present solutions in the Indian context. To place this examination in context, the paper shall explain the reason which necessitates such examination. In the modern world, a director is appointed not only for his technical expertise but also for his networking skills, personal contacts, credibility, integrity and reputation. In such a

1 *Aas* v. *Benham* [1891] 2 Ch. 244.

2 (1726) Sel. Case. Ch. 61 (Ct of Chancery) (hereinafter *Keech*).

3 [1942] 1 All ER 378 (hereinafter *Regal*).

scenario, these skills often lead to several opportunities presenting themselves to the director, while he continues as a corporate character. Precluding all of these opportunities, without distinction, comes across as an untowardly strict rule which stifles directorial entrepreneurialism. In this light, examining corporate opportunity and the no conflict and no profit rules[4] which form the basis of how a director should conduct himself when faced with a corporate opportunity gain practical relevance.

II Contextualizing the director's duties as regards corporate opportunity

A variety of rules developed under common law and equity form the basis for precluding the director from exploitation of the information belonging to the company. The underlying principle is that when information is obtained by virtue of an individual's role as a director, the individual is obligated to use that information solely for the company's benefit.[5] Despite not being *stricto sensu* property, property has been interpreted to cover information in multiple instances.[6] As a result, information, treated as property, cannot be personally appropriated by the director.[7]

The scope of a director's duty as a trustee requires him to treat any information belonging to the company in equity as an asset of the company.[8]As a trustee of company property, the director is duty bound to act with a total absence of temptation in discharging obligations towards the assets.[9]Apart from the principles of trusteeship,[10] the prohibition on the use of corporate opportunity was influenced by the general fiduciary duty of loyalty. This duty obligates the fiduciary to render undivided loyalty to the company.[11] The fiduciary duty of loyalty is a foundation which finds expression

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4 Despite controversy over whether the no-conflict and no profit are different or whether the no profit rules are a part of the no conflict rules, the latter position is adopted. The activity sought to be prevented by the no-profit rules will necessarily overlap with the wider set of activities sought to be prevented by the no conflict rules. For that reason, the authors have ignored objective based differences to consider the no profit rules to be a part of the no conflict rules and deal with all cases as per that framework. Even s. 175 of the English Companies Act, 2006 which deals with the director's fiduciary duty to avoid a conflict of interest with the company considers the no-profit rules to be a part of the no-conflict rules. See Rebecca Lee, "Rethinking the Content of the Fiduciary Obligation" 73 *Conv.* 236 and 237 (2009). See Upjohn's position in *Boardman* v. *Phipps* [1967] 2 A.C. 46 which considers the no-profit rules as a sub-set of the no-conflict rules.

5 *Thomas Marshall (Exporters) Ltd.* v. *Guinle* [1979] Ch 227; *Fine Industrial Commodities Ltd* v. *Powling* (1954) 71 RPC 253; Robert R Pennington, *Company Law* 716-717 (Lexis nexis UK, 8th edn., 2001).

6 *Burland* v. *Earle* [1902] AC 83; *Cook* v. *Deeks* [1916] AC 554; *Cran leigh Precision Engineering Ltd* v. *Bryant* [1965]1 *WLR* 1293.

7 See John Lowry and Rod Edmunds, "The Corporate Opportunity Doctrine: The Shifting Boundaries of the Duty and its Remedies" 61 *Mod L Rev* 515-516 (1998).

8 *Gore Browne on Companies* I, 16-1-16-2 (Jordan Publishing Ltd., 44th edn., 2004).

9 *Whitcote* v. *Lawrence*, 20 E.R. 1248.

10 *Supra* note 8 at 16-1.

through multiple doctrines[12] central to the conduct of fiduciaries.[13]As succinctly expressed, 'the loyalty obligation is given content by the no-profit and no-conflict rules'.[14]A conflict between personal interests of the fiduciary and the company violates the core duty of loyalty[15] which forms the background rationale[16] to the development of these rules as the duty requires the fiduciary to work solely for the profitability of the company.[17]

Gower classifies fiduciary duties into six sub groups out of which three flow from the basic premise that fiduciaries cannot be placed in a position wherein personal interests conflict with their duty to the company.[18] The rule against utilization of corporate opportunity or information is one of the three. Acting due to motives of personal profit or advantage while in the capacity of a fiduciary indubitably violates equity and the extant proscription seeks to prevent such a violation. The rules regulating corporate opportunity fall into the wider genre of rules requiring the director to disclose any interest in a transaction by the company, limiting loans by the company to directors, appointment of directors' relatives to positions in the company and likewise provisions which aim to ensure that extraneous considerations do not clash with the fiduciary duties of the director.

Indian corporate structures usually blur the distinction between ownership and control. A group of shareholders, family or otherwise, control decision-making in many companies. In India, there are hardly any obstacles to diversion of company property such as opportunity or information for the benefit of other companies when those in control have interests in multiple companies. There is immense possibility of numerous unreported instances wherein directors use their discretion in using the corporate opportunity of a particular company without sole regard for that company's profitability. In this context, it becomes important for shareholders, enforcement agencies and directors to become aware of the rules governing corporate opportunity.

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11 *Bristol and West BS* v. *Mothew* [1998] Ch. 1.

12 Generally See P.D. Finn, "The Fiduciary Principle" in T.G. Youdan (ed.), *Equity, Fiduciaries and Trusts* 3, 20-28 (1989).

13 Mathew Conaglen, "The Nature and Function of Fiduciary Loyalty" 121 *LQR* 452, 480 (2005).

14 Andrew D. Hicks, "The Remedial Principle of Keech v. Sanford Reconsidered" 69(2) *CLJ* 290 (2010).

15 See Daniel J. Carr, "Equity Rising? Commonwealth Oil and Gas Co Ltd v. Baxter" 14(2) *Edin LR* 273 (2010).

16 See James Edelman, "When do Fiduciary Duties Arise?"126 *L.Q.R.* 317 (2010). As the duty of loyalty is invoked as the basis, all the fundamental justifications which this duty contains, support the framework of the no-conflict and no-profit rules.

17 Joseph E. O. Abugu, "Director's Duties and the Frontiers of Corporate Governance" *ICCLR* 322, 328 (2011).

18 L.C.B. Gower and Paul L. Davies, *Principles of Modern Company Law* 381 (Sweet and Maxwell, 7th edn., 2003).

Despite the importance of this issue, Indian courts have scantly considered the rules regulating the use of corporate opportunity. Guidance from English and US cases can help us arrive at a position in this regard.

III Beyond equity's inequitable result [19]

In English law, the law on corporate opportunity was codified for the first time in section 175 of the English Companies Act, 2006 which reads thus:

(1) A director of a company must avoid a situation in which he as, or can have, a direct or indirect interest that conflicts, or possibly may conflict, with the interests of the company.

(2) This applies in particular to the exploitation of any property, information or opportunity (and it is immaterial whether the company could take advantage of the property, information or opportunity).

(3) This duty does not apply to a conflict of interest arising in relation to a transaction or arrangement with the company.

(4) This duty is not infringed

(a) if the situation cannot reasonably be regarded as likely to give rise to a conflict of interest; or

(b) if the matter has been authorised by the directors.

(5) Authorisation may be given by the directors

(a) where the company is a private company and nothing in the company's constitution invalidates such authorisation, by the matter being proposed to and authorised by the directors; or

(b) where the company is a public company and its constitution includes provision enabling the directors to authorize the matter, by the matter being proposed to and authorised by them in accordance with the constitution.

(6) The authorisation is effective only if—

(a) any requirement as to the quorum at the meeting at which the matter is considered is met without counting the director in question or any other interested director, and

(b) The matter was agreed to without their voting or would have been agreed to if their votes had not been counted.

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19 Gower's comment on the result of the judgment in the iconic English case of *Regal (Hastings) Ltd. id.* 18, at 418. (b) the matter was agreed to without their voting or would have been agreed to if their votes had not been counted.

(7) Any reference in this section to a conflict of interest includes a conflict of interest and duty and a conflict of duties.

Years of common law jurisprudence influenced the content of section 175. However, only section 175(1) is incorporated into the Indian Companies Bill, 2012 as 166(4).[20] Given the absence of cases interpreting the provision, it is appropriate to undertake a detailed examination of the English cases which are considered to be the basis for the law on corporate opportunity.

Keech v. *Sandford* [21]

Keech is often cited as the earliest case standing for the proposition that property resulting from knowledge acquired in the capacity of a trustee becomes trust property.[22] In *Keech*, a person devised his lease in trust with an infant as the beneficiary. On expiry of the lease, extension of lease was refused for the infant. When it was clear that the lease could not be extended unless someone other than the infant renewed it, the trustee renewed it for himself. The trustee was held liable to account notwithstanding the lack of absence of good faith or damage to the person to whom the fiduciary obligation was owed.[23] This reasoning forms the basis of common law's rigorous rule wherein a profit arising out of activities which involve or could possibly involve a conflict of interest between the fiduciary and the company has to be accounted back to the company.[24] On the other hand, some authors have advocated a relaxed rule which involves a circumstance based determination contingent on multiple variables not limited to ability of the company to use an opportunity, nature of opportunity, motives of the director and the manner in which the opportunity presented itself.[25] It will be instructive to consider a few select cases used to support the strict approach before analyzing those cases which are considered to follow the flexible approach.

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20 The Companies Bill, 2012 is to be enacted as the Companies Act of 2013. S. 166(4) of the Companies Bill, 2012 is *in pari materia* with s. 175(1) of the English Companies Act, 2006.

21 *Supra* note 2.

22 In *Attorney General of Hong-Kong* v. *Reid* [1994] 1 A.C. 324, Templeman understood this to be the rule from *Keech*.

23 *Chan* v. *Zachariah* (1984) 154 *C.L.R.* 178. For a detailed analysis of *Keech*, see *supra* note 14, at 287-320.

24 Ernest Lim, "Director's Fiduciary Duties: A New Analytical Framework" 129 *L.Q.R.* 242-245 (2013).

25 *Id.* at 242. As Lim comments, most authors adopt this demarcation between the strict and the flexible approaches while analyzing issues involving corporate opportunity. For arguments on the flexible approach, see John Lowry and Jen Sloszar, "Judicial Pragmatism: Director's Duties and Post-Resignation Conflicts of Duty" *J.B.L.* 83- 86 (2008). This article offers an excellent analysis of how certain English cases move forward from the 'straightforward capacity-based approach' to dilute the inflexible and inexorable application of the rules with respect to use of corporate opportunity. Also supporting the flexible approach is R. Edmunds and J. Lowry, "The No-Conflict-No Profit Rules and the Corporate Fiduciary: Challenging the Orthodoxy of Absolutism" *J.B.L.* (2000).

Regal (Hastings) v. *Gulliver*[26]

Regal involved a company which owned a cinema hall and wanted to purchase two others. For such a purchase, a subsidiary company was incorporated. Though the subsidiary was initially supposed to issue only £2000 as capital, conditions imposed for leasing out the other two theatres required each of Regal's directors, Regal's chairman and the solicitor to subscribe for 500 £ 1 shares each[27] apart from Regal taking up 2000 £ 1 shares. A while later, all the shares in both the companies were sold. A profit was made on the sale. The purchaser of Regal's shares sought to recover the profit made on the 3000 £ 1 shares sold by the former directors and others[28] on the ground that such a profit accrued from a fiduciary relationship. Upholding the purchaser's claim against the former directors, Russell[29] reiterated that the rule obligating fiduciaries to account for profit is not dependent on absence of bona fides, fraud or whether at all the company would have otherwise received the profit but simply on the mere fact of a profit accruing while acting as a fiduciary.

This judgment can be criticized on two grounds. First, the reason behind Gower's characterization of the strict rule in *Regal* as inequitable which is that the decision's only impact was to create an 'undeserved windfall' for the purchasers by effectively reducing the purchase price of the shares and resulting in recovery in favor of the wrong people.[30] Secondly, the argument that the judgment prioritized form over substance. From Sealy, it is clear that liability would not have been attracted if the company's approval had been obtained at the general meeting.[31] Since it is evident that the company was incapable of subscribing for more than 2000 £ 1 shares, the directors merely needed approval from the general meeting to take up the remaining shares. Given that they exercised control over the general meeting, it was a procedural formality.

At present, the basis for the second objection would not stand upon a correct understanding of the vexed issue of ratifiability.[32] It is submitted that an artificial distinction cannot be drawn between the exercise of a proprietary right by the director as a shareholder and what is owed to the company as a fiduciary duty. Thus, even if the directors could ratify their diversion of company property by virtue of also being majority shareholders, equity demands that such ratification cannot be validated.

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26 *Supra* note 3.

27 In sum, they together subscribed for a total of 3000 £ 1 shares.

28 One is not concerned with the holding as regards the chairman and the solicitoras they did not act as fiduciaries.

29 Porter agreed with the final conclusion while Macmillan, Wright and Viscount Sankey concurred with Russell.

30 *Supra* note 18 at 416-418.

31 Len Sealy and Sarah Worthington, *Cases and Materials in Company Law* 316 (Oxford University Press, 8thedn., 2008).

32 The authors do not seek to analyze what are 'unratifiable wrongs' but whether or not the directors can ratify their wrongs while acting in the capacity of shareholders.

Despite *Burland*[33] and *North-West Transportation Co Ltd.*[34] cases attesting to the importance of a shareholder's voting right and the capacity of the majority to ratify by exercise of voting power, the author uses *Menier* case[35] and subsequent developments[36] to recommend that a director who diverts information or opportunity belonging to the company cannot ratify the act in his capacity as a shareholder at the general meeting. As Buckmaster puts it, 'directors holding a majority of votes would not be permitted to make a present to themselves'.[37] Therefore, an authorisation by non-interested members at the general meeting, after having decided to not use the opportunity or information for the company, is a pre-requisite for the director to take up an opportunity under the rigor of common law.

Industrial Development Consultants v. *Cooley*[38]

Industrial Development Consultants applied the strict approach enunciated in *Regal*. In this case, a skilled managing director got relieved from his position by citing ill-health. The reason behind his departure was to take up a contract with the gas board which came to his knowledge while serving as the managing director. The gas board, despite his efforts, absolutely refused to contract with the company but evinced interest in contracting with him personally.

Roskill J held the managing director liable to account as he 'put his personal interest as a potential contracting party … in direct conflict with his pre-existing and continuing duty as managing director'.[39] Liability was attached due to the managing director's failure in not conveying the information received in his personal capacity to the company. The fact that the gas board would not have contracted with the company and that the fiduciary is now accounting for profit which the company could not have made even if the fiduciary duties were performed was considered by the court but rejected as having no bearing upon the wider application of the no-conflict rule.[40] The broad manner in which the no-conflict rule was stated followed from expanding upon *Regal* and *Keech*. Years later, Collins J in *CMS Dolphin* v. *Simonet*[41] identified the principled basis in *Industrial Development Consultants* as diversion of an opportunity which the company was pursuing[42] rather than failure to disclose information gained

33 *Burland* v. *Earle* [1902] AC 83 (Privy Council)

34 *North-West Transportation Co Ltd* v. *Beatty* (1887) 12 App Case 589 (Privy Council).

35 *Menier* v. *Hooper's Telegraph Works* (1874) 9 Ch App 350.

36 See s. 239, English Companies Act which disenfranchises the wrongdoing shareholder from voting in the capacity of a shareholder to ratify his wrongs.

37 *Cook* v. *Deeks* [1916] 1 AC 554 (Privy Council).

38 [1972] 2 All ER 162 (hereinafter, *Industrial Development Consultants*).

39 *Supra* note 8 at 16-9- 16-10.

40 *Supra* note 18 at 419.

41 [2002] B.C.C. 600.

42 Whether or not the company could achieve the opportunity is immaterial.

in a private capacity. From *CMS Dolphin*,[43] it is also clear that resignation from a company to pursue a corporate opportunity is no defense to a director's liability for appropriation of the corporate opportunity. *Industrial Development Consultants*[44] lease stands on the basis that the managing director allowed a conflict of interest before the end of his fiduciary obligations.

Bhullar v. *Bhullar*[45]

Bhullar is a relatively recent reiteration of the strict approach. In this case, differences developed between two factions of a family who jointly owned and managed a business. They decided to part ways and pending negotiations, the board resolved to not acquire new property. In a private capacity, a member of one faction noticed a property for sale. This property was duly purchased by a company solely controlled by this faction of the family. The other faction contended that this purchase was appropriation of corporate opportunity. The court characterized the opportunity to acquire the property pending negotiations as a corporate opportunity.

The court held the directors liable by stating that they had 'at the material time, one capacity and one capacity only in which they were carrying on business, namely as directors of the company'. While they remained directors, they were deemed incapable of considering opportunities which the company could have pursued. *Bhullar* case[46] is specially significant as it emphatically upheld the traditional approach despite indications from some quarters[47] that a flexible approach should take over. The court understood the rules governing corporate opportunity as requiring the directors to communicate information relevant to the company, irrespective of whether or not the opportunity materialized for the company. While imposing such a positive duty to disclose on the directors lacks basis, such a requirement seems necessary whenever the director seeks to lawfully pursue an opportunity.[48] The clear thread running through *Bhullar* case[49] and *Industrial Development Consultants*[50] case is the foundational rule of preventing conflict of interest.[51] In *Bhullar* case,[52] the company was still functioning when the director brought the property as his own. The director cannot define his duty contingent on

43 *Supra* note 41.

44 *Supra* note 38.

45 [2003] EWCA Civ 424.

46 *Ibid.*

47 These cases will be considered later. *See Balston Ltd* v. *Headline Filters Ltd.*[1990] F.S.R. 385; *Framlington Group plc.* v. *Anderson* [1995] 1 B.C.L.C. 475 and *Island Export Finance Ltd.* v. *Umunna* [1986] B.C.L.C. 460.

48 For a detailed analysis of this issue, see Hans C. Hirt, "The Law on Corporate Opportunities in the Court of Appeal: Re Bhullar Bros Ltd" *J.B.L.* 676-682 (2005).

49 *Supra* note 45.

50 *Supra* note 38.

51 See Bryan Clark, "UK Company Law Reform and Director's Exploitation of Corporate Opportunities" *I.C.C.L.R.* 233-235 (2006).

52 *Supra* note 45.

whether the opportunity could be taken up by the company. As long as there is possibility, real or supposed, of the opportunity remaining 'commercially attractive' to the company, the director cannot pursue it without authorisation by the general meeting.[53]

Re Allied Business and Financial Consultants Ltd; *O' Donnell* v. *Shanahan*[55] marked the culmination of *Bhullar's* case[55] rejection to consider whether a company has an actual beneficial interest or not as a parameter for determining liability to account.[56] Directly applying *Regal*,[57] *O' Donnell*[58] emphasized on the importance of undivided loyalty, rejected arguments that the director was not liable as the opportunity was impossible[59] for the company to have taken up and affirms the position that any opportunity arising *qua* director cannot be pursued unless the general meeting provides informed consent.[60] This concludes the section on analyzing the cases which constitute the core of common law's rigorous approach.

IV Diluting the rigor: the shift towards pragmatism

Some cases have sought to depart from the strict approach laid down in foundational cases such as *Keech*[61] and *Regal*.[62] As opposed to the construction of a principle followed by specific analysis like the earlier section, the paper shall concentrate on the methods and relevant facts used by these cases for advancing an approach not adhering to the traditional position. It is important to note that these cases embark upon a fact specific scrutiny of whether or not appropriation of opportunity has been made out. By itself, this is a significant difference from the architecture of how the rule against conflict has been originally viewed. Prentice posits *bona fides* of directors' actions, source of information about the opportunity, rejection of opportunity by the board, commercial impossibility for company to take up an opportunity and consideration of opportunity after resignation as some of the heads under which directors claim defense against liability.[63] While none of them would have made a difference to a holding of liability if conflict existed under the traditional position, it is interesting to know how these factors influenced the courts in some cases.

53 For a sound and balanced defense of *Bhullar*, See D.D. Prentice and Jenny Payne, "The Corporate Opportunity Doctrine" *L.Q.R.* 198-202 (2004).

54 [2009] EWCA Civ 751 (hereinafter, *O' Donnell*).

55 *Supra* note 45.

56 Though involving a discussion based on common law, both *Bhullar* and *O' Donnell* involved a statutory unfair prejudice claim.

57 *Supra* note 3.

58 *Supra* note 54.

59 See S. Scott, "The Corporate Opportunity Doctrine and Impossibility Arguments" 66 *Mod L Rev* 852 (2003).

60 Deirdre Ahern, "Guiding Principles for Directorial Conflicts of Interest: Re Allied Business and Financial Consultants Ltd; O' Donnell v. Shanahan" 74 *Mod L Rev* 596-616 (2011).

61 *Supra* note 2.

62 *Supra* note 3.

63 *Supra* note 53.

In *Balston Ltd* v. *Headline Filters Ltd*.,[64] Falconer J refused to hold a director liable to account for forming the intention to start a competing business before his resignation took effect. Diluting the application of the broad rule in *Industrial Development Consultants*,[65] it was held that unless actual competitive activity happened while acting as a director, the rule against conflict does not stand violated by the director's decision to start a competing business before he demitted office.[66] In *Island Export Finance Ltd*. v. *Umunna*[67] which was considered in *Balston*,[68] Hutchinson J opined that prohibiting directors from an opportunity which fructified post resignation[69] merely because they came to know about the opportunity while being a director cannot be justified on policy grounds. The rationale behind the holding was that the experience gained by virtue of acting as a director cannot be wiped clean and such experience has the potential to lead to opportunities which the director can legitimately take up. *Foster Bryant Surveying Ltd*. v. *Bryant*[70] is a recent case which considered both the rigorous approach under common law and the evolving stance of flexibility. After surveying both positions, Rix LJ refused to hold the director liable for breach of fiduciary duty on two grounds.[71] Firstly, the director was excluded from functioning as a director in the company. Secondly, the opportunity concerned was a client-led initiative which did not involve any voluntary act by the director.[72] Labeling the result as a product of a sound approach which focused on merit-based solutions, the court sought to eliminate the imposition of unrealistic and inequitable obligations upon the director.[73]

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64 [1990] F.S.R. 385.

65 *Supra* note 38.

66 In *Framlington Group plc.* v. *Anderson* [1995] 1 B.C.L.C. 475 where a finding of no liability to account was reached, the court refused to impose a fiduciary obligation upon the director to disclose the terms of his new employment unless they were violative of his earlier service contract. It reasoned that the terms were remunerative in nature and did not constitute a business opportunity for the plaintiff company.

67 [1986] B.C.L.C. 460.

68 *Supra* note 64.

69 When the resignation was not meant to take up that opportunity.

70 [2007] EWCA Civ 200.

71 See Tony Singla, "Case Comment: The Fiduciary Duties of Resigning Directors" *Comp. Law.* 275, 275-276 (2007).

72 See "Case Comment: Foster Bryant Surveying Ltd v. Bryant: Breach of Fiduciary Duty Considered after Director had Resigned" *Co. L.N.* 4 (2008).

73 In both *Foster Bryant Surveying Ltd.* and *In Plus Group Ltd.* v. *Pyke* [2002] 2 BCLC 201, the court accepted the inflexible and inexorable application of the exacting rules of equity as authority under ordinary circumstances but sought to state that certain factual matrixes make it impossible to strictly apply those rules. Both the cases involved innocent resignation of a director forced by the acts of other directors without any abuse of company property. Despite this, post resignation profits were sought to be recovered citing strict technical application of the no-conflict principle. Forced by the facts, the court sought to adopt a merit-based solution.

The Australian case of *Queensland Mines* v. *Hudson*[74] adopted a flexible approach too. It was a hard case unlike the English cases where the facts were heavily skewed towards a finding of non-violation of fiduciary duty by the director. Two connected reasons influenced Scarman's ruling. Firstly, it was impossible for the company to have utilized the opportunity as there was no working capital. Secondly, the director presented all facts before the board. Although there was no authorization by the general meeting, it was evident that the shareholders were also aware of the director's actions.[75] In *Peso Silver Mines Ltd. (N.P.L.)* v. *Cropper*,[76] the Canadian Supreme Court considered two factors critical for arriving at the conclusion that the no-conflict principle was not breached.[77] Firstly, the information was of a general nature and the managing director came across such information in a private capacity and not while acting in the specific capacity of a director.[78] Secondly, the board refused to pursue the opportunity following which the managing director took it up when approached.[79] As the discussion indicates, these decisions hinged on specific facts which were considered to merit a departure from the traditional position. It is now prudent to examine the US position wherein the methods used by the courts in cases which are considered to have adopted the flexible position find concrete exposition.

V Outlining the US position

Despite criticism about jurisdictional differences between states leading to lack of uniformity[80] in what one could term the 'doctrine of corporate opportunity' in the US, certain practical principles delineable from the US cases offer an alternative to English law.[81] The US courts decide upon the ownership of an opportunity before

74 (1978) 52 A.J.L.R. 399.

75 G.R. Sullivan, "Going it Alone: Queensland Mines v. Hudson" 42 *Mod L Rev* 711-715 (1979).

76 [1966] S.C.R. 673.

77 It must be noted that rejection of opportunity by the board or even authorisation by the board is irrelevant under the strict approach as utilization of corporate opportunity can only be permitted by the general meeting. However, the Company Law Review Steering Group, 2001 recommended that the board should be permitted to authorize a director to pursue a corporate opportunity is some specified instances. Mary Arden, "Reforming the Companies Acts-the Way Ahead" *J.B.L.* 579, 592-593 (2002).

78 Under common law, this factor cannot be considered as a director can act only as a director and not in any other capacity.

79 For an analysis of the *Peso Silver Mines* case *vis-à-vis* the traditional position and s. 175 of the UK Companies Act, 2006, See Jie Li, "The Peso Silver Case: An Opportunity to Soften the Rigid Approach of the English Courts on the Problem of Corporate Opportunity". *Comp. Law.* 68, 68-74 (2011).

80 David Kershaw, "Lost in Translation: Corporate Opportunities in Comparative Perspective" 25 *O.J.L.S* 603, 603-627 (2005).

81 For arguments suggesting that despite uniform underlying policy, conflicting tests have arisen on account of the flexibility in US law, see Victor Brudney and Robert Charles Clark, "A New Look at Corporate Opportunities" 94 *Harv L Rev* 997 (1981).

considering whether or not the director has exploited the corporation's property.[82] Agency forms the background for US cases on corporate opportunity.[83]

§ 5.05 of the American Law Institute Project on Corporate Governance, apart from attempting to provide clarity[84] on applicable rules, permits directors to utilize corporate opportunities and make profits provided such a corporate opportunity is disclosed and necessary ratification obtained.[85] The definition of corporate opportunity recognizes the distinction between an opportunity belonging to the corporation and an opportunity which can be legitimately exploited by the directors in a personal capacity.[86]

The rules regarding corporate opportunity in the US broadly involve three issues.[87] Firstly, the corporation's 'line of business'[88] and the opportunity's relation to it.[89] As *Guth* suggests, the line of business test covers those opportunities closely associated with the corporation's business or those opportunities which the company can utilize with its knowledge and experience.[90] Related to this issue is the real or expectant interest that a corporation might have in an opportunity.[91] Secondly, the corporation's practical and financial ability[92] to utilize the opportunity[93] and finally, the *fides* of the director who exploits a particular opportunity.[94] Cases on corporate opportunity deal

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82 See David Kershaw, "Does it matter how the law thinks about corporate opportunities?" 25 *O.J.L.S.* 533-558 (2005).

83 This means that in case the corporation (principal) is unable to pursue an opportunity, the director (agent) can do so in an individual capacity.

84 There is criticism to the effect that the flexible case-specific determination under American law leads to a loss of certainty. See Bryan Clark, "UK Company Law Reform and Director's Exploitation of Corporate Opportunities" *I.C.C.L.R.* 231, 236-237 (2006).

85 Christopher A. Riley, "The American Law Institute's Principle of Corporate Governance" *Comp. Law.* 122, 125-126 (1995).

86 Saleem Sheikh,"Corporate Governance: Reflections on the American Law Institute Report" *I.C.C.L.R.* 254, 258 (1995). See *Kaplan* v. *Fenton*, 278 A.2d 834 (Del. 1971).

87 See Marc J. Lane, *Representing Corporate Officers, Directors, Managers and Trustees* 5-24-5-31 (Wolters Kluwer Law and Business, 2nd edn., 2012).

88 As *Miller* v. *Miller* (1977) ALR.3d. 941 indicates, absent any reasonable connection to existing or prospective business of the company, the opportunity would not fall under the category of a corporate opportunity as it is not in the company's line of business.

89 R. Edmunds and J. Lowry, "The No-Conflict-No Profit Rules and the Corporate Fiduciary: Challenging the Orthodoxy of Absolutism" *J.B.L.* 122, 123-126 (2000). This classic piece elucidates the line of business test in detail.

90 *Guth* v. *Loft, Inc.*, 5 A. 2d 503 (Del. Ch. 1939). See G. Carrad, "The Corporate Opportunity Doctrine in Delaware: A Guide to Corporate Planning and Anticipatory Defensive Measures" 2 *Del J Corp L* 1 (1977).

91 *Equity Corp.* v. *Milton* 221 A2d 494 (Del. 1966).

92 *Supra* note 90.

93 Pat K. Chew, "Competing Interests in the Corporate Opportunity Doctrine" 67 *N.C. L. Rev.* 435, 470-471 (1989).

94 B. Pettet, *Company Law* 170 (Pearson Longman, 2nd edn., 2005). See *Broz* v. *Cellular Information Systems Inc* Del. Supr. 637 A2d 148 (1996) and *Thorpe* v. *CERBCO Inc.,* Del. Supr. 676 A2d 436 (1996).

with variants of these issues and the nature of these issues imparts flexibility to the US approach which appreciates the wealth of factual information surrounding a company's activities and rejects a strait-jacketed formula for determining liability of directors for exploitation of corporate opportunity.[95]

VI Discerning an Indian perspective

Vaishnav Shorilal Puri; Seaworld Shipping and Logistics Pvt. Ltd. v. *Kishore Kundanlal Sippy*[96] is the only Indian case to analyze the law on corporate opportunity.[97] It reflects a confused application of the English cases and the US position on corporate opportunity.

The facts clearly required a holding that the directors violated the no-conflict principle. To elucidate, the case involved two groups who were equal shareholders in a company. One group actively managed the company's affairs. Having acquired information and built relationships while acting as directors, the group managing the affairs diverted an unambiguous corporate opportunity to another company which it formed by itself.

The court applied section 88 of the Indian Trusts Act, 1882 to understand the duties owed by a fiduciary such as the duty of honesty, loyalty and disclosure.[98]

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95 *Supra* note 72 at 140.

96 [2004] 120 Comp Case 681 (hereinafter, *Vaishnav Shorilal*). This Bombay High Court decision was an appeal from the decision of the Company Law Board decision in *Kishore Kundan Sippy* v. *Samrat Shipping and Transport systems P. Ltd.*, [2004] 118 Comp Case 472.

97 However, the Income Tax Appellate Tribunal in *Assistant Director of Income Tax (International Taxation)*; *Ravinder Behl* v. *Ravinder Behl*; *Deputy Director of Income Tax (International Taxation)* directly applied, without any analysis or consideration of sources, the rule stated in the American Law Institute Project on Corporate Governance that the director should disclose about a corporate opportunity and first offer it to the corporation. Also, in *Liz Investment Private Ltd.* v. *Far Pavilions Tours and Travels Private Ltd.*. [2006] 130 Comp Case 449 (CLB), the Company Law Board used *Vaishnav Shorilal* to *prima facie* find that a corporate opportunity was taken away. The authors found that these are the only reported instances in which the law on corporate opportunity was considered by Indian courts or tribunals. Where a trustee, executor, partner, agent, director of a company, legal advisor, or other person bound in a fiduciary character to protect the interests of another person, by availing himself of his character, gains for himself any pecuniary advantage, or where any person so bound enters into any dealings under circumstances in which his own interests are, or may be, adverse to those of such other person and thereby gains for himself a pecuniary advantage, he must hold for the benefit of such other person the advantage so gained.

98 S. 88 of the Indian Trusts Act, 1882 reads: "Where a trustee, executor, partner, agent, director of a company, legal advisor, or other person bound in a fiduciary character to protect the interests of another person, by availing himself of his character, gains for himself any pecuniary advantage, or where any person so bound enters into any dealings under circumstances in which his own interests are, or may be, adverse to those of such other person and thereby gains for himself a pecuniary advantage, he must hold for the benefit of such other person the advantage so gained.

The principles laid down in cases such as *Industrial Development Consultants*[99] and *Regal*[100] were discussed in light of section 88.[101] The court then applied the landmark American case of *Guth*[102] and the principles laid down by the American Law Institute to determine that the director was liable for appropriating corporate opportunity. It examined whether the company was in a position to have taken up the opportunity and the *fides* of the directors concerned.[103] Though it would not have affected this case, it is necessary to note that the court applied the rigorous framework of common law to understand the application of some of the factors[104] relevant only under the US law. In effect, this would result in indirectly adopting the rigor of common law though the US position was used to determine liability but only for invalidating the relevance of certain factors under the US law. Given the absolute lack of jurisprudence in India on the law governing corporate opportunity apart from the inadequate treatment in *Vaishnav Shorilal*,[105] it is apt to understand section 166(4) of the Companies Bill, 2012 in light of the discussion in preceding sections.

VII Brief comment on the codified fiduciary duty to avoid conflicts of interest

The Indian Companies Bill, 2012 attempts to follow the approach of the UK Companies Act, 2006 by explicitly codifying the fiduciary duties of directors. Section 166(4) of the Companies Bill, 2012 encapsulates the no-conflicts principle. Since it is *in pari materia* with section 175(1) of the UK Companies Act, 2006, a discussion on the text of section 175 (1) will prove helpful. The other parts of section 175, codifying and in some cases, deviating from the common law rules governing corporate opportunity are not included in the bill. Given the absence of any Indian approach to dealing with issues involving corporate opportunity prior to section 166(4), either through statute or by case-law, it is submitted that this omission to include other parts of section 175 under the bill, 2012 is more inadvertent than conscious. If the intent behind section 166(4) was to merely state the broad no-conflict principle without coloring it with the details under section175, the resulting scope for judicial interpretation is problematic especially since section 175 appears to blend pragmatism without compromising on rigor.[106]

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99 *Supra* note 38.

100 *Supra* note 3.

101 Since the Bombay High Court affirmed the reasoning used by the Company Law Board to understand corporate opportunity, the analysis used by the Company Law Board is being treated as the analysis of the court.

102 *Supra* note 90.

103 A fact-based scrutiny which forms the basis of the flexible position was used.

104 Factors which are irrelevant under the traditional common law position such as financial capacity of the corporation or unwillingness of third parties to contract with the company are accorded due regard under American Law.

105 *Supra* note 96.

106 Given that there is little from past Indian cases to suggest any method of interpretation.

Section 175 (1) is considered to reflect the strict traditional approach of common law.[107] It imposes a positive obligation to avoid conflicts of interest thus imposing a greater burden than was the case under the traditional position which did not include such a positive obligation.[108] As Buckley puts it, disabilities are now cast as duties.[109] Other parts of section 175 modify extant common law by permitting the board to authorize exploitation of a corporate opportunity by a director in certain instances.[110] While several authors have commented upon the provisions of section 175,[110] such opinions mostly concern other parts of section175 as section 175 (1) is considered a straightforward embodiment of the principles laid down in foundational English cases such as *Keech*,[112] *Regal*[113] and *Industrial Development Consultants*.[114] Given the clear absence of the other parts of section 175 under Indian law, it is impermissible to draw any conclusions for India on the basis of anything except section 175 (1) which is only a reiteration of the principles applicable under the rigor of English law.

VIII Conclusion

The marked lack of engagement by the Indian courts with the law on corporate opportunity needs to be remedied. Even the Companies Bill, 2012 inexplicably omits most parts of the now codified English position. Apart from an adequate understanding of the traditional UK cases and cases considered to advocate a pragmatic dilution from the rigor of the traditional position, the flexible doctrine of corporate opportunity adopted by the US courts should inform any interpretation that is sought to be placed upon the no-conflicts principle codified in section 166(4) of the Companies Bill, 2012. The authors undertake to submit the existing framework and the varied approaches used by courts to provide an informed discussion of the law on corporate opportunity to aid adjudication when issues arise in Indian courts. Certain factual

107 The text appears to have been influenced by *Aberdeen Railway Co* v. *Blaikie* (1854) 1 Macq. 461, a case which supports the rigor of the foundational principles enunciated in *Keech*.

108 *Supra* note 24 at 243.

109 *5 Buckley on the Companies Act*, 3-35-3-36 (Lexis Nexis Butterworths, 2008).

110 See s. 175 (4), s. 175 (5) and s. 175 (6).

111 See Deirdre Ahern, "Legislating for the Duty on Directors to Avoid Conflicts of Interest and Secret Profits: The Devil in the Detail" *Irish Jurist* 82, 82-106 (2010); Majed Sanat Alsulais Alotaibi, "Regulating Conflicts of Interest in Post-CA 2006 Era: Part 2: is Authorisation by the Board a Good Innovation" *I.C.C.L.R.* 351, 351-356; Jie Li, "The Peso Silver Case: An Opportunity to Soften the Rigid Approach of the English Courts on the Problem of Corporate Opportunity" *Comp. Law*. 68, 68-74 (2011); Mark Hsiao, "A Sprouting Duty of Honesty and Loyalty? Companies Act 2006" *I.C.C.L.R.* 301, 301-308 (2009); Ernest Lim, "Director's Fiduciary Duties: A New Analytical Framework" 129 *L.Q.R.* 242-245 (2013).

112 *Supra* note 2.

113 *Supra* note 3.

114 *Supra* note 38.

matrixes like those in *Foster Bryant Surveying Ltd.*,[115] *Island Export Finance Ltd.*[116] and *Balston*[117] present a clear case for relaxing the prophylactic exacting standards underscored in cases such as *Keech*[118] and *Regal.*[119] A proper scrutiny of the factors influencing a finding of no liability for directors in both commonwealth jurisdictions and the US present the judiciary with tools to evolve commercially sensible and legally justifiable solutions. Without departure from the background principles forming the basis of the traditional position, manifestly unreasonable results can be avoided.

S.V. Joga Rao *

*Y. Shiva Santosh Kumar***

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115 *Supra* note 70.

116 *Supra* note 67.

117 *Supra* note 64.

118 *Supra* note 2.

119 *Supra* note 3.

* M.L., M. Phil., Ph. D., Max-Planck fellowship (MPI-Freiburg, Germany)Formerly, Professor of Law, National Law School of India University, Bangalore & Dean and Professor of Law, Rajiv Gandhi School of Intellectual Property Law, IIT Kharagpur.

** IVth Year BA. LL.B. (Hons.), National Law School of India University, Bangalore.