

Directors & Officers Liability Insurance

The following cases are just a few real life examples of how a director and principal officer can be exposed to the risk of regulatory inquiries and court actions undertaken by zealous regulators and uncontrollable shareholders. These cases will show to you why every director in Asia is in need of a high quality and comprehensive Directors & Officers Liability Insurance (D&O) Policy.

Kelon Litigation in China

Kelon Electrical Holdings (“Kelon”) is a company based in Guangdong province, and was once China’s biggest airconditioning and refrigerator manufacturer, which is listed on both the Hong Kong and Shenzhen stock exchanges. In about June 2005, the China Securities Regulatory Commission (CSRC) launched a fraud investigation against Kelon and its directors. Kelon’s former chairman, Gu Chujun and eleven other Kelon executives were dismissed in August 2005. The investigation found out that Kelon overstated its profits by RMB387,000,000 (US\$47,000,000) and revenues by RMB1,200,000,000 (US\$153,000,000).

CSRC, pursuant to the new Securities Law of China (which came into effect on 1 January 2006) impose fines against both Kelon and Gu. Kelon was fined RMB600,000 (US\$75,000) for providing false information and some other offences whilst Gu was fined RMB300,000 (US\$37,500) for a number of “economic crimes”.

On the other hand, recovery actions have also been initiated by Kelon’s subsidiaries against Gu in 2006 seeking RMB332,000,000 (US\$42,000,000). The disgruntled shareholders also later joined forces by filing a lawsuit against Kelon in July 2006 seeking significant civil damages. The suit which was instituted on behalf of the minority shareholders was lodged with the Guangzhou Intermediate People’s Court against Kelon and Kelon’s former auditor. These claims against Kelon will obviously be the first landmark case for minority shareholders protection. An announcement was issued on 2 April 2008 indicating that the Yangzhou and Jiangxi subsidiaries have successfully obtained judgments from the PRC courts against Gu.

Lawsuit against President of a Computer Game Company in Korea

A Korean website company filed a class action against a Korean computer game company (“Game Company”) and its president on behalf of a number of people who had their respective resident registration numbers and personal information stolen. Their identities were illegally used by others to sign up for the online game developed by the Game Company although they have not themselves signed up for the game operated by the Game Company.

The plaintiffs alleged that the Game Company and its president were under obligations to prohibit use of a stolen name by the applicant. It was also alleged that they have been negligent in not verifying the user's real name and personal information. More than 8,000 plaintiffs were involved in the class action. Each of the plaintiffs sought damages in the sum of KRW1,000,000 (US\$960). The class action was dismissed by the Court and the plaintiffs have appealed.

US Class Action lodged against Directors of 51job.com

A US law firm filed a class action in the United States District Court for the Southern District of New York on behalf of all securities purchasers who had acquired shares of 51job.com, a Chinese company engaging in human resources business between 4 November 2004 and 14 January 2005. The complaint charges the company together with three directors and officers with violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934.

They were alleged to have failed to disclose adverse facts by misrepresenting or recklessly disregarding adverse material known to the defendants. Such information includes unpleasant profit outlook as a result of improperly recognized recruitment advertising revenue. The defendants lodged a motion to dismiss the complaint. In November 2006, the Court entered an Order dismissing the action with prejudice. Substantial defence costs have been incurred by the defendant directors.

Breach of Fiduciary Duties in Singapore

The plaintiff was a company providing business management consultancy services. The first defendant was the founder of the plaintiff company in which he was a director and shareholder. The second defendant was the Chief Executive Officer of the plaintiff.

The plaintiff sued the defendants for breach of fiduciary duties. The thrust of the plaintiff's action was that the defendants conspired and conducted activities in conflict with their duties to the plaintiff. It was alleged that the defendants have established another consulting company in December 2005 to compete with the plaintiff for its business. The defendants allegedly have also taken steps to persuade the plaintiff's staff to join the new company whilst at the material time still acting as the officers of the plaintiff.

In May 2008, the Singapore High Court found that the Defendants have taken steps to plan their exit from the plaintiff. They have talked to many employees and clients, shortly forming the vehicles for competition. The Court held that the defendants were in breach of their fiduciary duties. The Court took the view that they were obliged, at the least, not to conduct activities that they ought to have known was or would be detrimental to their employer.

Dismissal of a Chairman in Hong Kong

A disgraced Chinese entrepreneur who fled China after being accused of economic crimes and being dismissed by his company brought proceedings against the company and some of the directors.

The company is a major vehicle maker in China and listed on the stock exchange of Hong Kong. In October 2002, the former chairman of the company brought a claim in the Labour Tribunal of Hong Kong demanding payment of approximately US\$4,300,000 with respect to loss of salary plus bonuses, share options and damages for alleged unreasonable dismissal. The claim was dismissed by the Labour Tribunal but was later transferred to the High Court of Hong Kong. Several directors were named as defendants in addition to the company. The proceeding has not yet been resolved.

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