DIRECTORS' DUTIES & RESPONSIBILITIES (SINGAPORE)

Robson Lee
Partner

GIBSON, DUNN & CRUTCHER LLP
One Raffles Quay
#37 01 North Tower
Singapore 048583

GIBSON DUNN

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1. INTRODUCTION

While it is an honour to be nominated and elected to a company's board of directors, the position comes with serious duties and responsibilities. Most prudent businessmen will not hesitate in refusing to guarantee a friend's loan; however, they will readily fall for the dubious prestige of being invited on to the board of a company, sometimes with results infinitely more damaging.

This paper highlights a director's duties imposed under the Act, the Listing Manual of the SGX and the Take-Over Code.

More importantly, the regulatory climate of directors' duties is evolving in Singapore. The CA Amendments was enacted in October 2014, after the MOF reviewed the comprehensive recommendations of a SC appointed by the MOF to revamp the Act.

The CA Amendments will be implemented in two phases – the first phase from 1 July 2015 and the second phase from Q1 2016. This paper will highlight the changes that have been implemented as well as those that will come into force in Q1 2016.

The Take-Over Code is also set to be amended. On 6 July 2015, the SIC issued a consultation paper proposing the Take-Over Code Amendments. This paper highlights the material changes under the Take-Over Code Amendments that clarify the duties of the offeree board in a take-over situation.

2. DIRECTORS' ROLE

A company is an artificial legal entity. Its legal existence is recognised only by reason of parliamentary legislation under the Act.

The distinguishing characteristic of a company from a natural person is that it is capable of perpetual existence unless liquidated, dissolved or removed from the Register of Companies. A company comes into existence by incorporation within the requirements of the Act. Accordingly, a company has its own legal persona. It is capable of suing and being sued in its own name, regardless of the persons who may in fact be "owners" in the sense of being shareholders, or "operators" and "managers" in the sense of being directors or managers.

A company, not being a natural person, cannot act on its own. It can only act through its directors and other officers who have been given the necessary authority and power either to act as the company or on behalf of the company. The Act implicitly recognises this by requiring every company to have at least one director (S. 145(1)). This is so even if the company is a wholly owned subsidiary of another holding company. If a company has only one member, the sole member can also be the sole director of the company.

The authority and powers of directors are usually set out in the articles of association of the company, which the company may draw up on its own or adopt Table A. The articles usually provide that the business of the company shall be managed by the directors (for example, see Article 73 of Table A). The point to emphasise is that the directors who exercise the authority and powers conferred on them by the articles must act as a board (unless delegated in the manner permitted by the articles) and that their acts are considered the acts of the company rather than the personal acts of directors.

The role and functions of directors have always been difficult to define. The law as a whole has taken a pragmatic approach in not attempting to formulate an exhaustive list of the matters that only directors can discharge. As a matter of practice, the role and functions of directors would vary from company to company and it would largely depend on the arrangements of the internal management structure adopted by the company concerned.

Perhaps the general functions of directors may be described as follows, to quote from an address given in 1972 by Sir Robert Crichton Brown, President of the Australian Institute of Directors:

"In practice, it can be said that the board is responsible for laying down matters of principle, and of accounting, statistical and management procedures. It is responsible for the decision of what products to make, of what markets to go into, of what manufacturing capacity is required, or how spare capacity should be utilised, of investment decisions, of the development of its property, the purchase of capital assets, the return of funds, as to where funds should be invested, cash flow and of course liquidity.

The director is concerned with performance, with the proposals and budgets that are brought up by management. He is concerned with performance within those budgets, the funds required for those budgets; if the funds are not used, he will want to know why; if more funds are used, he will want to know why. He is concerned with performance of the various divisions or units within a company and with turnover and the return on funds. He is concerned as to financial commitments, whether committed, possible or probable, whether immediate, short term or long term and should try to look five years or further ahead. He is concerned with the major contracts and obligations that the company may enter into. In brief he is concerned to see that top management effectively does its job, that proper reports are made and information given."

Whilst there is a wide variation of the role and functions actually performed by the board of directors, certain areas of responsibility are generally accepted:

(a) to establish and implement basic objectives and broad policies of the company consistent with its objects as set out in the memorandum and articles of association of the company;

(b) to elect officers of the company and to advise, approve, supervise and review the actions and performance of such officers;

(c) to acquire, dispose of, charge and safeguard the assets of the company;

(d) to approve important or major financial matters and to ensure that proper reports are given to the shareholders;

(e) to delegate special powers to others on matters requiring board approval;

(f) to maintain, revise and enforce the memorandum and articles of association of the company; and

(g) to establish and perpetuate a sound board of directors.

3. DIRECTORS DEFINED

3.1. Identifying the Directors of a Corporation

Under the Act, a "director" is defined broadly, as any person occupying the position of director of a corporation by whatever name called. The Act further defines "director" to include an alternate or substitute director as well as a person in accordance with whose directions or instructions the majority of the directors of a corporation are accustomed to act.

In most cases, it should not be difficult to identify a director of the company. This is usually done by conducting an instant information search at ACRA. Companies are required to notify the Registrar of ACRA within one month of any appointment or change in the appointment of directors. The CA Amendments reduced this period to 14 days. These changes will come into effect in Q1 2016.

Within the company itself, the identity of its directors can be ascertained by:

(a) examining the Register of Directors;

(b) examining the resolutions of the board and the company expressly appointing persons as directors to the board; or

(c) examining the BizFile "Endorsement by Director for Appointment" statement (formerly known as Form 45), which a company is required to file online with ACRA when a director is appointed.

3.2. Executive Directors

The first species of directors are the ones we are most familiar with. They are known as executive directors and they work for a company on a more or less full-time basis. It is usual for executive directors to enter into service agreements with the company. A managing director is an executive director who is in charge of managing the company.

3.3. *De facto* Directors

A *de facto* director is a person who acts as a director even though he was never appointed as such. It would be a question of fact whether a person has assumed the role, functions and responsibilities of a director in the company, notwithstanding that such person may not in fact have been formally appointed as a director of the company. In Raffles Town Club Pte Ltd v Lim Eng Hock Peter and others (Tung Yu-Lien Margaret and others, third parties) (2010), Justice Chan Seng Onn undertook an extensive review of past cases and derived the following propositions:

(a) to establish that a person was a *de facto* director of a company, it is necessary to plead and prove that he undertook functions in relation to the company which could properly be discharged only by a director;

(b) it is not a necessary characteristic of a *de facto* director that he is held out as a director; such "holding out" may, however, be important evidence in support of the conclusion that a person acted as a director in fact;

(c) holding out is not a sufficient condition either, as what matters is not what he called himself but what he did;

(d) it is necessary for the person alleged to be a *de facto* director to have participated in directing the affairs of the company;

(e) the person in question must be shown to have assumed the status and functions of a company director and to have exercised "real influence" in the corporate governance of the company; and

(f) if it is unclear whether the acts of the person in question are referable to an assumed directorship or to some other capacity, the person in question is entitled to the benefit of the doubt.

Accordingly, a person who assumes the role of a director in a company is subject to the same duties and obligations of a formally appointed director, even if he has never been formally appointed.

It would appear that only the company has the power to bring legal proceedings against the *de facto* director to restrain him from continuing to act as a director of the company.

In practice, the situation of a *de facto* director arising is due to a defect or insufficiency in the procedure or formality of appointment, or due to the director not meeting or ceasing to meet certain qualifications for his appointment as director, or due to a person continuing to act as a director notwithstanding the termination of his appointment as a director.

Third parties dealing with the company have no means of ascertaining whether the person that they are dealing with is in fact a properly appointed director. Accordingly, the courts have devised a rule that *de facto* directors can bind the company to transactions that they have entered into with third parties who, acting in good faith, had reasonably believed that such directors have been properly appointed by reason of the fact that such directors are in control of the company's affairs. The third party can assume that the internal procedures and requirements of the director's appointment have been satisfied, unless there are suspicious circumstances that reasonably ought to put him on notice or inquiry.

S. 151 of the Act reinforces this rule by expressly providing that the acts of a director shall be valid notwithstanding any defect that may afterwards be discovered in his appointment or qualification.

Directors cannot, however, escape liability arising from their defective appointment by relying on the fact that they were not aware that their appointment was defective.

3.4. Alternate or Substitute Directors

The articles of association of a company usually contain provisions permitting directors to appoint another person as his alternate or proxy. Such alternate directors could then act in the place of the principal directors appointing them. He is considered to be a full director by the law and not just a mere agent of the person who appoints him, and can thus be made fully liable for any consequences that may arise in his capacity as an alternate director.

Notwithstanding that alternate directors can be appointed, the Governance Code promulgates the guideline that the company should avoid approving the appointment of alternate directors except for limited periods and in exceptional cases. Where alternate directors are proposed to be appointed, alternate directors should also be familiar with the company's affairs and appropriately qualified.

While compliance with the Governance Code is not mandatory, listed companies are required under the Listing Manual to disclose their corporate governance practices as well as explain any deviations from the Governance Code in their annual reports.

3.5. Additional Directors

The articles of association of a company usually empower the board to appoint further directors, in addition to the number already appointed, as well as to fill up casual vacancies in the board of directors.

3.6. Associate Directors

Article 94 in Table A provides that directors may, from time to time, appoint any person to be an associate director and, from time to time, cancel any such appointment. The distinguishing characteristic of an associate director from a director is that he does not have any right to attend or vote at any meeting of directors except by the invitation and with the consent of the directors.

It is unclear whether associate directors fall within the definition of directors under the Act. An associate director may fall within the definition if he has assumed the role of director in the company. The fact that the associate director does not have any right to attend or vote at any meeting of directors may go some way towards supporting the argument that he does not occupy the position of director.

The purpose of appointing associate directors is to allow certain individuals selected by the directors to understudy the role and functions of the directors with a view to subsequently appointing them formally as directors.

3.7. Shadow Directors

A shadow director would fall under the definition of a director under an Act because he would be a person in accordance with whose directions or instructions the *majority of the* directors of a company are accustomed to act. The current version of the Act contains no definition of shadow director. However, the foregoing definition can be found in its predecessor, the Companies Act (Cap. 50, 1994 Rev. Ed.). The italicised terms were in the CA Amendments which came into effect on 1 July 2015. S. 4(2) was also revised to clarify that a professional adviser will not be regarded as a shadow director merely because the majority of the directors are accustomed to act on his advice.

Justice Chan Seng Onn, in Raffles Town Club Pte Ltd v Lim Eng Hock Peter and others (Tung Yu-Lien Margaret and others, third parties) (2010), explained that the difference between a *de facto* director and a shadow director is that, unlike the former, the latter does not claim or purport to act as a director. In fact, he claims not to be a director but is actually controlling the board of directors from behind the scenes.

The court in Re: Hydrodam (Corby) Ltd (1994) laid down four requirements which have to be proved in order to establish a shadow-directorship and the liability of a shadow director:

(a) who the directors of the company were, whether *de facto* or *de jure*;

(b) that the alleged shadow director instructed the directors on how to manage the company;

(c) that the directors acted in accordance with his instructions; and

(d) that they were accustomed to so act.

Under the Interpretation Act, a person is defined to include a company. Given a literal interpretation of the definition of directors in the Act, a holding company may be said to be a shadow director of its subsidiaries, as in most cases, the directors of the subsidiaries would be accustomed to act in accordance with the directors or instructions of the holding company. Indeed, in the Australian case of Standard Chartered Bank of Australia Ltd v Antico (1995), the court found that a holding company with only 42% shareholding in a company was a shadow director as it had exercised extensive management control over the company and the other significant shareholders held, respectively, only 10%, 6%, 6% and 3% of the company's shares.

An alternative view is that the directors of the holding company may be deemed to be shadow directors of its subsidiaries.

On a literal reading of the definition of directors under the Act, it would appear that shadow directors are subject to the same statutory obligations under the Act as directors. Otherwise, the duties and liabilities that are imposed by law on directors may be circumvented through the unscrupulous use of shadow directors. It must be the intention of the law that no one is to escape the duties and liabilities of being a director if one is indeed acting as one, even if one was never formally appointed as such and prefers to remain behind the scenes.

The SC recommended in its Report that it is not necessary to have a separate definition of "shadow director" in the Act as the existing definition of "director" already encompasses shadow directors. It also recommended that the Act should clarify that a person who controls the majority of the directors is to be considered a director. This is because it would be unrealistic to subject a person who controls only one director to all the obligations and duties of a director. The SC cautioned that doing so would result in corporate shareholders who nominated directors to the board of companies being regarded as shadow directors. This may lead to corporate shareholders owing duties of care to one another in closely held joint venture companies. The MOF has accepted both of the SC's recommendations. This is reflected in the revised S. 4(1) of the Act.

3.8. Nonexecutive Directors

Non-executive directors do not work for the company on a full time basis. Frequently, non-executive directors are nominees of major shareholders whose main task is to keep a close eye on the managers and executive directors in order to safeguard their investment. Indeed, the Governance Code expressly states that nonexecutive directors should constructively challenge and help develop proposals on strategy, and review the performance of management in meeting agreed goals and monitor the reporting of performance.

3.9. Independent Directors

Independent directors are a subset of nonexecutive directors and whose rise to prominence stems from the increased focus on corporate governance. It should be noted that while the Act has no concept of independent directors (though S. 201B(2) alludes to it), and the Listing Manual only makes one reference to independent directors (see Rule 704(8) of the Listing Manual), independent directors form an integral part of the board of a listed company.

The Governance Code defines an independent director as a director who has no relationship with the company, its related corporations[1], its 10% shareholders[2] or its officers that could interfere, or be reasonably perceived to interfere, with the exercise of the director's independent business judgement with a view to the best interests of the company. Examples of relationships which are relevant to the question of independence include past employment by the company, and dealings between the director's immediate family[3] with the company.

Under the Governance Code, independent directors should be identified in the company's annual report. The company's Nominating Committee (as defined below) is charged with the responsibility of determining annually, and as and when circumstances require, if a director is independent.

Importantly, one of the principles promulgated by the Governance Code is that there should be a strong and independent element on the board, which is able to exercise objective judgment on corporate affairs independently. The Governance Code recommends that independent directors should make up at least one-third of the company's board, and half where:

(a) the Chairman and the CEO is the same person;

(b) the Chairman and the CEO are immediate family members;

(c) the Chairman is part of the management team; or

(d) the Chairman is not an independent director.

Where any of the four situations listed above occurs, the Governance Code also states that the company should appoint an independent director as the lead independent director. He should also be available to shareholders where they have concerns for which normal channels to the Chairman, CEO and/or chief financial officer have failed to resolve or would be inappropriate.

The Governance Code recommends rigorous review of the independence of any director who has served more than nine years from the date of his appointment, and that the board of the company should explain why such a director should be considered independent.

Lastly, it should be noted that while compliance with the Governance Code is not mandatory, under the Listing Manual, listed companies must disclose their corporate governance practices in their annual reports and explain any and all deviations from the guidelines of the Governance Code.

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1 "related corporation" means a corporation that is the company's holding company, subsidiary or fellow subsidiary.

2 "10% shareholder" means a person who has an interest or interests in one or more voting shares in the company and the total votes attached to that share, or those shares, is not less than 10% of the total votes attached to all the voting shares in the company. "Voting shares" exclude treasury shares.

3 "immediate family" means a person's spouse, child, adopted child, step-child, sibling and parent.

4. APPOINTMENT OF DIRECTORS

The Act does not prescribe the manner in which directors are to be appointed. Frequently, the articles of association provide for this and directors are usually appointed at the company's AGM. Thus, the present position is that the company's articles will provide for the appointment of directors, or the default position in Table A will apply unless it is excluded by the company's articles. A new S. 149B of the Act was introduced in the CA Amendments to allow the appointment of a director by ordinary resolution passed at a general meeting, subject to any contrary provision in the articles. These changes will come into effect in Q1 2016.

A principle of the Governance Code is that the process for the appointment of directors should be formal and transparent. It recommends the establishment of a Nominating Committee which should comprise of at least three directors, the majority of whom, including the Nominating Committee's chairman, should be independent.

In selecting and appointing or re-appointing directors, the Governance Code recommends that the Nominating Committee should consider the composition and progressive renewal of the board and each director's competencies, commitment, contribution and performance (e.g. attendance at meetings, preparedness, participation and candour). The Governance Code also provides that a description of the process for the selection, appointment and re-appointment of directors should be disclosed in the company's annual report.

The Governance Code also recommends that all directors be required to submit themselves for re-nomination and re-election at regular intervals and at least once every three years.

5. QUALIFICATIONS AND DISQUALIFICATIONS OF DIRECTORS

5.1. Essential Qualifications (S. 145(2))

A person must satisfy the following qualifications before he can be appointed a director:

(a) He must be a natural person. Accordingly, a company cannot be appointed a director (but see comments on shadow directors above);

(b) He must be at least 18 years of age; and

(c) He must have full legal capacity. While "full legal capacity" is not defined in the Act, this can generally be taken to mean a person who has the necessary legal capacity to give or take lands and other things or to maintain legal actions. For example, it can generally be said that a person who is of unsound mind does not have the necessary legal capacity and accordingly under the Act an insane person does not qualify to be appointed a director.

The Act prescribes no other mandatory qualifications or requirements, or that a director should possess any particular educational qualification or business experience. In their recent review of the Act, the SC and MOF reiterated that the Act should not prescribe the academic or professional qualifications of directors or mandate the training of directors generally, given that there is no compelling reason to do so. Notwithstanding this, it should be borne in mind that under the Governance Code, key information regarding directors, such as academic and professional qualifications, experience and other commitments, should be disclosed in the company's annual report.

Statutory requirements aside, a company may provide in its memorandum and articles that a person must satisfy certain conditions before he may be appointed as a director, for example, that he must own at least a certain number of shares in the company.

While the Act does not require much to become a director, it does provide for a list of situations whereby a person may be disqualified from or unqualified for the post of director. Examples are:

(a) failure to lodge a 'consent to act as director' form and a statement that he has not been disqualified from acting as a director, with ACRA (S. 146(1A));

(b) failing to hold share qualifications within two months of appointment if the articles of association requires such share qualification (as discussed below) (S. 147);

(c) acting as a director or manager without the leave of the court while an undischarged bankrupt (S. 148); and

(d) being a disqualified and unfit director of an insolvent company or a company that is being wound up (S. 149).

The CA Amendments introduced an additional disqualification (pursuant to a repealed and re-enacted S. 155A), which will, from Q1 2016, provide for an automatic five-year disqualification if a director was a director in at least three companies which were struck off by ACRA within a five year period.

5.2. Share Qualifications (S. 147)

The Act does not require a person to hold any shares of a company before he can be appointed as its director. The articles of association of the company may, however, specify that a director must hold a specified number of shares.

The Act provides that a person must obtain his qualification shares within two months, or any such shorter period as may be prescribed by the articles, of his appointment as director.

If a person appointed as a director fails to obtain his qualification shares within the requisite period or ceases to hold his qualification shares, he is required to vacate his office as director.

This means that the failure by a director to observe the share qualification requirement does not automatically terminate his appointment as director. Further steps, albeit minor, are required to be taken to terminate his appointment as director. A fine not exceeding $4,000 and a default penalty is imposed if the requirement to vacate the office of director is not complied with.

5.3. Disqualifications

The following categories of persons would commit an offence under the Act if they act as directors.

(a) **Undischarged bankrupts (S. 148)**

It used to be that a person who is an undischarged bankrupt, whether made a bankrupt by a Singapore or foreign court, shall be guilty of an offence if he acts as a director or participates in the management of a company without leave of court. The court in Re Altim Pty Ltd (1968) explained that the purpose of this disqualification is to protect the public on the basis that a person who is an undischarged bankrupt is *prima facie* not a fit person to be entrusted with the management or direction of a company, especially a company with limited liability.

However, S. 148 of the Act has been amended such that an undischarged bankrupt is now allowed to participate in the management of a company as long as the leave of the court or written permission from the Official Assignee is obtained.

The prohibition extends to the situation where such a person is directly or indirectly taking part in or concerned in the management of a Singapore or foreign company.

If convicted of an offence under this section, the penalty is a fine not exceeding $10,000 or to imprisonment of a term not exceeding two years or both.

(b) **Unfit directors of insolvent companies (S. 149)**

The court is empowered to make an order disqualifying a person from acting as a director or taking part in or concerned with the management of a company for a duration not exceeding five years.

The disqualification order is made if the court is satisfied that the person:

(i) is or has been a director of a company which has, at any time, gone into liquidation and was insolvent at that time, if such person was a director at the time of liquidation or had ceased to be a director within three years of the liquidation, and

(ii) the conduct of the person as a director, either only in relation to the company under liquidation, or taken together with his conduct as a director of other company or companies, renders him unfit to be a director of or take part in or be concerned with the management of a company.

In deciding whether a person is unfit to be a director by reason of his conduct as a director, the court shall consider:

(i) in general:

  (1) whether there has been any misfeasance or breach of fiduciary or other duty by the director to the company;

  (2) whether there has been any misapplication or retention of, or any conduct by the director giving rise to an obligation to account for, any monies or other property of the company;

  (3) the extent of the responsibility for any failure by the company to comply with S. 138 (keeping copies of charging instruments and register of charges), S. 190 (keeping a register of members), S. 191 (place where register of members is to be kept), S. 196B (information to be provided by pre-existing private companies)[4], S. 197 (annual returns), S. 199 (accounts to be kept) and S. 201 (accounts, consolidated accounts and directors' report);

(ii) in particular:

  (1) the extent of the responsibility for the causes leading to the company's insolvency;

  (2) the extent of the responsibility for any failure by the company to supply any goods or services which have been paid for whether in whole or in part;

  (3) the extent of the responsibility for the company entering into any transaction which may be set aside under S. 259 (prohibition against disposition of property of the company after commencement of winding up); and

  (4) whether the causes of the insolvency of the company are attributable to the business of the company being in a particular industry where the risk of insolvency is generally recognised to be higher.

The person need not be convicted of an offence or be criminally liable in respect of any of the matters set out above.

The director, however, does not vacate office automatically and must resign from office. A person who acts as a director after a disqualification order has been made against him shall be guilty of an offence. Upon conviction such a person shall be

[4] New insertion under the CA Amendments which will come into force in Q1 2016.

liable to a fine not exceeding $10,000 or to imprisonment of a term not exceeding two years or both.

A person subject to disqualification may, however, apply to the court for leave to take part in or be concerned with the management of a company. Please note that the Act does not expressly permit him to apply to the court for leave to act as a director.

(c) **Conviction of Certain Offences (S. 154)**

A person who has been convicted of certain offences in Singapore or elsewhere would have committed an offence if he acts as a director or takes part in or is concerned in the management of a company for five years after conviction or, if imprisoned, after his release from prison. S. 154 was also revised following the CA Amendments. These changes came into effect on 1 July 2015.

The offences are:

(i) any offence involving fraud or dishonesty punishable on conviction with imprisonment for three months or more;

(ii) any offence under Part XII (market conduct) of the SFA or the imposition of a civil penalty under S. 232 of the SFA;

(iii) any offence in connection with the formation or management of a corporation; and

(iv) any offence under S. 157 (duty to act honestly and diligently, and prohibition against improper use of information) or S. 339 (keeping of proper accounts).

If convicted of an offence under this section, the penalty is a fine not exceeding $10,000 or to imprisonment of a term not exceeding two years or both.

Two types of disqualifications are provided under S. 154: automatic disqualification and disqualification by court order. S. 154 makes a distinction between fraud and dishonesty on the one hand and management offences on the other. Disqualification is automatic in the former class of cases where the director is convicted of an offence involving fraud or dishonesty punishable with imprisonment for three months or more. It has been suggested that if a person is convicted of an offence he will be disqualified if his criminal acts in fact involve fraud or dishonesty, *even if the prosecution is not obliged to prove fraud or dishonesty* to secure a conviction.

Under the CA Amendments, the automatic disqualification regime for directors convicted of offences involving fraud or dishonesty has been retained in the Act. However, directors who are automatically disqualified are now allowed to apply to the High Court for leave to act as a director or take part in the management of the company. To provide guidance on the scope of offences involving fraud or dishonesty, a non-exhaustive list of offences will be made publicly available. The MOF has accepted the SC's recommendation on this matter.

In the latter class of cases involving offences connected with the formation or management of a corporation, or any offence under S. 157 or 339, disqualification is subject to the prosecution's application and presumably, the court may also, by its own motion, impose it as one of the sentencing options. No guidelines have been given as to what offences are deemed to be in connection with the 'formation or management of a corporation', but it is unlikely that S. 154 applies only to offences under the Act. Any offence committed by a director or manager in the exercise of his executive powers in relation to a company, whether punishable under the Act or under some other statute, will probably be an offence in connection with the management of the company. The court will probably have to find a nexus between the offence and the formation or management of the company.

The court in Quek Leng Chye v Attorney General (1985) took pains to explain that S. 154 is not punitive in nature but is for the protection of the public, members of the company, creditors and others who deal with limited liability companies.

(d) **Persistent Default in Delivering Documents (S. 155)**

A person commits an offence if he acts as a director, promoter or takes part in or is concerned in the management of a company if:

(i) he has been persistently in default of the requirements under the Act; and

(ii) has within a period of five years been convicted of any offence or subject to an order under S. 13 (duty to make returns) or S. 339 (keeping of proper accounts).

A person is deemed to be persistently in default if he has, within five years, been convicted of three or more offences in relation to such requirements under the Act or has three or more orders made against him under S. 13 or S. 339.

The disqualification is not automatic and the person under disqualification must resign from directorship. He may apply for leave to the court to act as a director or to take part in or be concerned in the management of a company.

If convicted of an offence under this section, the penalty is a fine not exceeding $10,000 or to imprisonment of a term not exceeding two years or both.

(e) **Being a director in not less than three companies which were struck off within a five-year period (S. 155A)**

As discussed, the repealed and re-enacted S. 155A will come into force in Q1 2016. Under S. 155A, an automatic five-year disqualification term will be imposed if a director was a director in at least three companies which were struck off by ACRA within a five-year period. The five-year disqualification period starts after the last of the three companies were struck off. A disqualified director may apply to the Court for leave during the period of disqualification to act as company directors or take part in the management of a company.

S. 155A will only apply to companies that are struck off on or after the date of commencement of this provision in Q1 2016.

If convicted of an offence under this section, the penalty is a fine not exceeding $10,000 or to imprisonment for a term not exceeding two years or both.

5.4. Age Limit

The CA Amendments removed the age limit of 70 years for directors under the current S. 153 of the Act. This change is also expected to come into effect in Q1 2016. The SC noted that persons above 70 years of age can be capable of doing the job of a director and are often re-appointed in practice. There is also no age limit for directors in the United Kingdom (“**UK**”), Australia, New Zealand and Hong Kong. The MOF agreed with the SC on this and is of the view that it is best to allow the shareholders to decide whether to approve the appointment of a director.

5.5. Articles of Association

The articles of association of a company may also provide for the disqualification of persons from acting as directors. The more common conditions for disqualifications are:

(a) insanity;

(b) resignation by written notice to the company;

(c) absence from meetings without permission from directors for more than six months; or

(d) failing to declare the nature of interest in any contract with the company.

5.6. Effect of Disqualification

A person who is disqualified under paragraphs 5.3(a) or (d) does not stand automatically vacated from his office as director. Further steps (albeit minor) must be taken to terminate his appointment as director. In particular, he must resign and refrain from participating in the management of companies for the prescribed period. But whilst he remains a director, the person under disqualification will continue to commit an offence under the Act.

Given that the sections do not provide for automatic vacation of office, the acts of the disqualified director must still be binding on the company. It is settled law that an outsider is not required to check whether a company's directors have been properly appointed (Royal British Bank v Turqand (1855)) as it would be unfair to creditors and other third parties dealing with the company if a transaction with a company is held to be void because they did not know that the director had been disqualified. Furthermore, S. 151 provides that the acts of a director shall be valid notwithstanding any defect that may afterwards be discovered in his appointment or qualification.

5.7. Application for Leave of Court to Act as Director

A person who is disqualified from acting as a director under paragraphs 5.3(a) to (e) above may apply to the court for leave to act as a director (subject to the qualification in paragraph 5.3(b)).

Matters that the court may take into consideration in deciding whether to grant leave includes:

(a) the nature of the offence that the applicant has been convicted of, in the case of a conviction under S. 154 (see paragraph 5.3(c));

(b) the nature of the person's involvement;

(c) the person's general character;

(d) the structure of the company which the person seeks to be a director of;

(e) the nature of the business of the company that the person seeks to be a director of;

(f) the interests of the general public, the shareholders, the creditors and the employees of the company that the person seeks to be a director of;

(g) the risks to the general public, the shareholders, the creditors and the employees of such company should the person be permitted to be a director; and

(h) in some cases, the court will take into account public sentiment such as public outrage in the event leave is granted.

6. REMUNERATION

6.1. Provision and Improvement of Director's Emoluments

The Act (S. 169) prohibits the provision or improvement of emoluments for directors in respect of their office unless it was approved by a resolution not related to other matters. Emoluments includes fees and percentages, sums paid by way of expenses allowance, contributions to pension and any benefits otherwise than in cash given to directors in respect of their services as directors.

6.2. The Remuneration Committee

The Governance Code provides that no director should be involved in setting his own remuneration. Instead, the company's board should set up a Remuneration Committee with written terms of reference. The Remuneration Committee should comprise at least three directors, the majority of whom, including the Remuneration Committee's chairman, should be independent. This is to prevent any potential conflicts of interest and possible breach of fiduciary duties (see below). The determination of a director's remuneration should be formal and transparent and the company's annual report should disclose the members of the Remuneration Committee and its key terms of reference.

The Remuneration Committee will then recommend to the board a framework of remuneration and the specific remuneration packages for each director and the CEO. The recommendations, which should contain all aspects of remuneration including director's fees, salaries, allowances, bonuses, options and benefits in kind, will then be submitted to the entire board who will review it.

6.3. Remuneration Package

The remuneration package should be attractive enough to attract, retain and motivate directors to run the company successfully. However, companies should avoid paying excessive salaries, something which may attract negative sentiment by shareholders or even the public, which occurred in the case of the National Kidney Foundation. The remuneration package should ideally be performance-based, such as the inclusion of performance incentives and profit hurdles before a bonus can be paid. Indeed, the Governance Code has as a guideline that a significant proportion of executive directors' and key management's remuneration should be structured so as to link rewards to corporate and individual performance, which should in turn be measured against appropriate and meaningful yardsticks. Where such long-term incentive schemes take the form of grants of options, shares or other deferred remuneration, the Governance Code further encourages the use of vesting schedules whereby only a portion of benefits can be exercised and/or paid out each year.

In the case of non-executive directors, the fact that they do not actively participate in the management of the company should go towards the decision on their remuneration package. Factors to be taken into account include effort and time spent on the company, as well as the level of responsibility of the nonexecutive director. Nonexecutive directors should not be overcompensated such that their independence can be called into question.

In all cases, the Governance Code recommends that companies adopt contractual claw-backs which will allow the reclamation of remuneration in exceptional cases of mismanagement and misconduct resulting in financial loss to the company.

6.4. Disclosure on Remuneration

The Governance Code provides that a company should disclose its remuneration policy, level and mix of remuneration, and the procedure for setting remuneration in its annual report. This will enable investors to understand the nexus between a director's remuneration and performance. Where short-term or long-term incentive schemes exist, the company should also set out a description of the performance conditions and explain why such key performance indicators were chosen.

The company should also report to the shareholders each year, the remuneration of all directors and at least the top five key executives (who are not directors or the CEO) in bands of $250,000. A breakdown of the remuneration, such as base salary, bonus, etc, should be provided.

The Governance Code further recommends that for transparency, the annual report should disclose details of the remuneration of employees who are immediate family members of any director, and whose remuneration exceeds S$50,000 during the year. Additionally, details of the relevant relationship will have to be disclosed.

6.5. Golden Handshakes

As is the case with the provision of emoluments, the Act (S. 168) prohibits a company from giving compensation to a director for loss of office, or as consideration for or in connection with his retirement from such office, unless particulars with respect to the proposed payment have been disclosed to the company's shareholders and approved by the company at a general meeting.

That said, in Grinsted Edward John v Britannia Brands (Holding) Pte Ltd (1996), the Court of Appeal approved the Australian case of Lincoln Mills (Australia) Ltd v Gough (1964) and held that not every payment made to a director upon the cessation of his employment would fall within the Act. Much would depend on the circumstances and the nature of the payment.

The requirement in S. 168 for shareholders' approval for the payment of compensation to directors for loss of office is retained in the CA Amendments.

A new exception has been introduced in the Act removing the need to obtain shareholders' approval where the payment of compensation to an executive director for termination of employment is provided in an agreement between the company and the director. The amount of the compensation must not exceed the total emoluments paid to such director in the past one year and disclosure is made to shareholders upon or prior to the payment of such compensation.

If disclosure is not duly made to shareholders, the amount received by the director shall be deemed to have been received by him in trust for the company. These changes came into effect on 1 July 2015.

7. FIDUCIARY DUTIES OF DIRECTORS

7.1. Introduction to Fiduciary Duties

The assumption by a person of the office of a director in a company carries with it the assumption of duties, responsibilities and liabilities that arise by reason of the attributes of the office imposed under the common law and by statutes.

The functions of directors require them to:

(a) exercise their powers conferred upon them under the articles of association of the company as directors; and

(b) have control of the property and assets of the company.

The general principles that govern the duties of directors have evolved through time by English judges dealing with issues brought before them for resolution and they are, to put it simply:

(a) the exercise by the directors of their powers as agents of the company; and

(b) the control of the property and assets of the company as trustees of the company.

The general principles governing the duties of agents and trustees are fairly well established. Inevitably, English judges have applied these principles by analogy, imperfect though they may be, to directors. The analogies are imperfect as:

(a) the acts of directors are acts of the company in some instances and are those of agents of the company in other instances; and

(b) the directors do not have title to the property and assets of the company as they belong to the company, and in this sense, the directors do not hold the property and assets of the company as trustees in favour of the company.

However, the common thread existing in the duties of trustees, agents and directors is that they each act not for their own personal benefit but for the benefit of third parties. Hence, there is the danger of abuse or misapplication of the powers conferred on them to the detriment of such third parties. As a result, the common law has placed fiduciary duties on directors to compel them to act in such a manner that is just and fair to such third parties.

In the recent decision of TYC Investment Pte Ltd v Tay Yun Chwan Henry (2014), Lee Kim Shin JC noted that directors are fiduciaries who must act in the best interests of the company. The

High Court opined that shareholders of a company are generally not subject to fiduciary obligations.

Accordingly, it has been often stated, in broad terms, that a person who is subject to fiduciary duties must act in good faith and with reasonable care and diligence. Fiduciary duty is the highest duty of care which the law can impose. The duty-holder must subordinate his own interests in preference for the beneficiary's in the event of a conflict.

7.2. Duty to Act in Good Faith

The phrase "good faith" has been used interchangeably with the phrases "honestly" and "*bona fide*", the latter being the Latin equivalent of the phrase "good faith". As then Chief Justice Chan Sek Keong observed in Townsing Henry George v Jenton Overseas Investment Pte Ltd (in liquidation) (2007), the duty of honesty and the duty to act *bona fide* may be regarded as a composite obligation.

Whether the phrase "good faith", "honestly" or "*bona fide*" is used or preferred, the crux of the matter is that any and every act or omission of a person in his capacity as a director of a company must be in the interests of the company. What the interests of the company, the shareholders, the employees and the creditors are, and whether the decision reached would be in their interests, is left to the judgement of the directors. Although this appears to be a subjective test (i.e., what did the director honestly believe was in the interests of the company), in practice, an objective test is used. In Heap Huat Rubber Company Sdn Bhd and Others v Kong Choot Sian and Other (2004), Justice Lai Kew Chai, sitting in the Court of Appeal, affirmed the court's earlier judgment in Intraco Ltd v Multi-Pak Singapore Pte Ltd (1995), that the test is whether an honest and intelligent man in the position of the directors, taking an objective view, could reasonably have concluded that the transactions were in the interests of the company.

The Act further reinforces the fiduciary duties imposed on directors under common law by the enaction of S. 157(1), which requires a director to always act honestly in the discharge of the duties of his office.

The section does not replace the common law obligations of directors but supplements them. It also imposes both civil and criminal sanctions on directors breaching the provisions of S. 157(1) by providing that:

(a) the director shall be liable to the company for any profit made by him or for any damage suffered by the company; and

(b) he shall have committed an offence and on conviction, be subject to a fine not exceeding $5,000 or to imprisonment of a term not exceeding one year.

As observed by Justice Selvam in Kumagai-Zenecon Construction Pte Ltd and Another v Low Hua Kin (1999), these sanctions are not unique to company law but stem from a long line of cases on directors' fiduciary duty. A fiduciary is liable to make full restitution and compensation if he breaches his fiduciary obligations. The wronged party must also be restored to the same position as he would have been if no breach had been committed.

It is pertinent to note that the SC has considered a proposal to decriminalise a breach of the directors' duties under S. 157 in its Report but found it appropriate to retain the current position in order to discourage any potential misconduct. This continues to be reflected in the CA Amendments to S. 157 which came into effect on 1 July 2015.

In applying S. 157, the court will adopt an objective standard of care. Hence, a director's inadequacy will only be relevant as a mitigating factor in sentencing.

7.3. Duty to Act in the Interests of the Company

(a) The Company

The counterpart of the duty of a director to act honestly and in good faith is to act solely to promote and protect the interests of the company as a whole. In reviewing the director's exercise of discretion, the court in Vita Health Laboratories Pte Ltd v Pang

Seng Meng (2004) upheld the rule that a court will not substitute their own judgement for that of the directors, especially with the benefit of hindsight. As Judicial Commissioner V K Rajah observed in that case, the courts will be slow to interfere with *bona fide* commercial decisions taken by directors and it is the role of the marketplace and not the function of the court to punish and censure directors who have, in good faith, made incorrect commercial decisions. Directors can take risks if they honestly believe it to be in the interests of the company, and an inference of dishonesty will only be made if the risk proved palpably unreasonable (Cheam Tat Pang v Public Prosecutor (1996)). In other words, generally, the court will not play directors, and will not invalidate business decisions unless the exercise of discretion was not made *bona fide*.

The case of Walker v Winborne (1975) illustrates the point that directors will be in breach of their duties to act in good faith of a company if they elevate anyone else's interest above that of the company. Here, the directors of a company ("**Asiatic**") also administered other companies of which they were directors of as a group. The directors caused Asiatic to loan money to other companies without interest or security. The Australia High Court held that the directors were in breach of their duties because they had to consider Asiatic's interests alone when deciding whether to lend money to other companies.

(b) **The Shareholders**

Inextricably bound to what is in the interests of the company are considerations of what is in the interests of the shareholders as a whole. S. 159 of the Act provides that the directors are entitled to have regard to the interests of the shareholders in exercising their powers. This, however, does not mean blindly conforming to the wishes of the majority. As the court in Greenhalgh v Arderne Cinemas Ltd (1951) said, directors must act in the interests of the company "as a whole". In a situation where the directors have exercised their powers in disregard of the interests of the shareholders, the Act gives dissatisfied shareholders (even minority shareholders) the right to apply to the court for an order under S. 216 or S. 216A (discussed in paragraph 14 below) that may include:

(i) the direction, prohibition, variance or cancellation of any transaction or resolution;

(ii) the regulation of the conduct of affairs of the company in the future;

(iii) the authorization of civil proceedings to be brought in the name of the company;

(iv) the purchase of the shares or debentures of the company by other members or holders of debentures of the company or by the company itself;

(v) in the case of a purchase of shares by the company provide for a reduction accordingly of the company's capital; or

(vi) the winding-up of the company.

In most cases, the commercial and business interests of a company would coincide with the interests of the shareholders. There may, however, be situations where the decisions of the directors have fulfilled the interests of the company but have a different impact on the interests of the shareholders or on different classes of shareholders.

The discharge of the directors' duty must involve due consideration being given to the interests of the company and the shareholders as a whole. The decision to adopt a particular course of action involves the exercise of business judgement which, as mentioned above, the courts will not interfere with. The courts will only intervene if it is shown that the directors have acted in bad faith, intending to prejudice the interests of the shareholders or certain classes (or factions) of shareholders, or that no sensible board of directors would have come to the decision which the directors have reached after taking into account the alternative options available to the directors. What the court can do is to declare the director's decision void or ineffective due to a defect in the decision making process itself (for example, the use of improper considerations like the intention to prejudice certain groups of shareholders, or the failure to adopt the proper procedure prescribed by law or in the articles and memorandum), rather than the contents of the decisions itself.

If there is a conflict of interests among various classes or factions of shareholders, then the issue is resolved by determining what is fair between the different classes or factions of shareholders and not what is in the interest of the company as a whole. Sometimes this can be resolved by determining what the predominant interest of the majority of shareholders in a given situation is, and the directors must decide the action to be undertaken by the company that would best serve that predominant interest with the least harm to the interest of the other shareholders.

(c) **Employees**

Following the decision in Parke v Daily News Ltd (1962), where the directors of a company approaching insolvency were found to have breached their duties when they passed a resolution distributing large sums of money to employees out of philanthropy, companies became wary of making corporate donations or gifts to employees.

However, the enactment of S. 23 and S. 24 of the Act expressly permits corporate donations and the power to make provision for employees and ex-employees in connection with the cessation of business.

As further reinforcement that companies can take into consideration the effect on their employees, S. 159 further provides that directors, in exercising their powers, are entitled to have regard to the interests of the company's employees, members and the rulings of the Securities Industry Council on the interpretation of the principles and rules of the practice to be followed under the Take-Over Code.

There are no case law authorities on the effect of this section, and any comments thereon would be speculative. As a preliminary comment, perhaps the directors, when taking into account the employees' interests, cannot give it more weight or precedence over the interests of the shareholders as a whole. It should also be noted that the section uses the permissive word "entitled" as opposed to the mandatory word "shall", which may suggest that this section does not impose a compulsory duty on the directors to take into account the interests of the employees. Hence, while directors can take into account employees' interests when making decisions, they are not required to do so under the Act.

(d) **Creditors**

When the company is not insolvent, creditors' interests are quite irrelevant. However, the same cannot be said as the company approaches insolvency.

In Chip Thye Enterprises Pte Ltd v Phay Gi Mo (2004), the court stated that the law recognises a duty by directors to present and future creditors if a company is insolvent or "put in a situation where its creditors will be prejudiced". The court in Tong Tien See Construction Pte Ltd v Tong Tien See (2001) explained that the rationale for this is that, as a company approaches insolvency, there may be no value in the company left for the residual claimants. Because of the incentive problems that are faced by all the shareholders, clearly some concern must be shown for the interests of the creditors. Hence, if the directors act in a manner that prejudices the creditors in such a situation, they may be guilty of misfeasance.

S. 339(3) of the Act makes it an offence for a director to contract a debt knowing that there is no reasonable or probable expectation that the company would be able to repay it. S. 340 further makes it an offence for directors to carry on the business of a company with intent to defraud its creditors. Importantly, under S. 340, the court can declare the director to be personally responsible, without any limitation of liability, for all or any of the debts or other liabilities of the company (see for example Tong Tien See Construction Pte Ltd v Tong Tien See & Ors (2001)).

It should be emphasised that where directors take into account the interests of creditors, it should not have more weight or precedence over the interests of the shareholders as a whole. It was stated by the High Court of Australia in Spies v The Queen (2000) that it is contrary to principle that directors owe an *enforceable, independent duty* to creditors.

It should be noted that the onset of insolvency entitles creditors to appoint a liquidator, which puts an end to the power of directors to manage a company. In fact, the Court of Appeal in Liquidators of Progen Engineering Pte Ltd v Progen Holdings Ltd (2010) recently affirmed the decision of the High Court in Chip Thye Enterprises Pte Ltd v Phay Gi Mo (2004) that when a company becomes insolvent, the interests of creditors become the dominant factor in what constitutes “the benefit of the company as a whole”.

The recognition that the interests of creditors have to be taken into account *only when a company approaches insolvency* does not in any way dilute the focus of directors’ duties. However, the suggestion by Lord Templeman in Winkworth v Edward Baron Development Co Ltd (1987) that directors may have to take into account the interests of *potential creditors* appears to weaken the enforceability of directors’ duties.

It has been argued that it is not the function of company law to encourage companies to adopt socially desirable behaviours, which should be within the purview of upstream regulations, such as those protecting employees or the environment. Creditors have other means of protecting themselves, such as the taking of security and rules providing for the maintenance of capital.

(e) **The Group**

Because the companies in a group are considered separate legal entities, the theoretical position is that directors of one company in a group should only take into account that company’s interests when making decisions.

In reality, however, it is not realistic to require the boards of subsidiaries to consider only the subsidiaries’ interests because, very often, the management and functions of the various subsidiaries and parent company are inextricably interwoven.

The court in Intraco Ltd v Multi-Pak Singapore Pte Ltd (1995) stated that it is permissible for directors to consider the interests of the group as a whole when making decisions, as long as they do not sacrifice the interest of any company within the group. The reason for this is that each company within the group has its own separate set of creditors. As long as it is not recognised that the creditors of a subsidiary have a right of recourse against the holding company in the event of default, the subsidiary cannot be sacrificed for the good of the group.

The directors of a company within the group can consider the company’s wider interests as a member of the group. For example, an unsecured interest-free loan by one company to another company at no interest would not be commercially justified. However, where the lender is a holding company and the borrower is a subsidiary, the holding company’s wider interest will include ensuring that its subsidiaries are solvent and the loan would thus be permitted (note however that S. 163 prohibits a company from making a loan to a subsidiary if the subsidiary is controlled by a director in a holding company, see 10 below).

7.4. Duty to Use Powers for the Proper Purpose

Directors are under a duty to exercise the powers vested in them by the memorandum and articles of association of the company and by the shareholders in the general meetings for the purposes for which the powers were conferred. This duty appears to be another expression of a wider duty that the directors must act in good faith and in the interests of the company and the shareholders as a whole.

If the directors exercise their powers for any other purpose, then any action or transaction arising from the exercise of such powers is voidable. The company may choose to declare it void or to adopt it and the directors may be liable to compensate the company for any loss it suffers as a result thereof. It is immaterial that the director acted honestly or that he considered the transaction to be in the interests of the company.

To illustrate this point, in the case of Re Duomatic Ltd (1969), a payment was made to an ex-director as compensation for loss of office. This was not disclosed to shareholders as required under the UK's Companies Act. Hence, it was not one that could lawfully be made. The court directed that the directors who authorised the payment be made liable on the grounds of misapplication of the company's funds. This was so even though the court found that they had acted honestly and out of ignorance of the law. More recently and closer to home, in the case of Panweld Trading Pte Ltd v Yong Kheng Leong and others (Loh Yong Lim, third party) (2012), a director was found to have breached this duty to use his powers for a proper purpose by making salary payments to his wife, who was never an employee of the company.

Some of the powers that are invariably conferred on the directors in the articles of association are the power to allot shares, to refuse to register transfers of shares, to make calls on shares, to forfeit shares, to pay interim dividends, to borrow and to make donations from company funds.

Accordingly, the directors must observe the prohibitions, restrictions and statements of purpose in the memorandum and articles of association when exercising their powers.

Where the purposes are not expressed in the memorandum and articles of association, then the court will have to infer the proper purpose from the context in which the power was conferred to the directors.

Another illustration of an improper exercise of power is the case of Howard Smith Ltd v Ampol Petroleum (1974). Howard Smith and Ampol were both trying to take control of a company ("**Miller**"). The directors of Miller considered that it would be in the interest of the company to be taken over by Howard Smith. However, Ampol, who had shares in Miller, used its voting power to block Howard Smith's bid. To get around the problem, the directors used their power to issue new shares to Howard Smith, which diluted Ampol's voting power. Even though the directors of Miller had the power to issue the shares, and even though Miller needed the money, the court held that the shares were issued for an improper purpose. It was improper because the reason for issuing the shares was to allow Howard Smith to take over Miller, notwithstanding that the directors of Ampol were honestly trying to advance the interests of the company. The Privy Council held that the power to issue shares was for the purpose of raising money for the company, not to forestall a takeover bid and hence was an abuse of power.

As the directors are under a duty to exercise their powers for the benefit of the company and the shareholders as a whole, they are prohibited from delegating their powers or agreeing to fetter the future exercise of their powers in the absence of express authority granted by the memorandum and articles of association or the shareholders in general meeting.

Where the directors had exercised their powers for an improper purpose, they may be liable under S. 157 of the Act that imposes criminal sanctions and in addition, the directors may be personally liable, under S. 157 and under common law, to the company to compensate for the loss suffered by the company by reason of the exercise of their powers for an improper purpose.

A side rule that may arise from this is the duty imposed on the directors not to exceed their powers. Where directors exceed the powers conferred on them, it would appear that they are liable to compensate the company for any loss suffered by reason thereof.

7.5. Special Problems of Nominee Directors and Directors Who Are Shareholders

The reference to nominee directors, in the strict sense, means a person who has been nominated and appointed to the board of directors by another person who may or may not be a shareholder of the company. It could also be extended to include directors who feel committed to some faction of shareholders or to some other third party.

Notwithstanding the fact that a person may be appointed as a director to represent a special interest, he is under a duty to exercise his powers and to act in such a manner that is in the interests of the company and the shareholders as a whole. As Justice Lai in W&P Piling Pte Ltd (in liquidation) v Chew Yin What and others (2007) explained, the law makes no distinction between duties owed by different directors, and a nominee director is thus under the same duties as other directors.

As a matter of law, once appointed as a director of the company, a director's duty to the company takes precedence over all other duties which he may owe to the party who had nominated him (although this is commercially unrealistic because, in practice, nominee directors are usually employees of the principal). The courts have iterated time and time again that nominee directors cannot place their appointer's interests above that of the company; nominee directors cannot be mere "watchdogs" (Justice Chao, Oversea-Chinese Banking Corp Ltd and another v Justlogin Pte Ltd and another (2004)). Where no conflict arises, it is clear that the nominee director may take into account the principal's interest.

Further difficulties encountered by the nominee director in the discharge of his duties relate to reporting back to his appointer. In this regard, if information disclosed to the appointer is confidential, the nominee director may be in breach of his duties to the company.

In this regard, Section 158 of the Companies Act previously allowed nominee directors to disclose to their appointers information acquired in their capacity as directors/employees only if authorised by the board of directors by a *specific* mandate. This mandate must contain specific details of the persons to whom disclosure is to be made and particulars of such information to be disclosed. These conditions have been relaxed considerably under the CA Amendments. Currently, Section 158 allows nominee directors to make such disclosure if the disclosure is authorised by the board of directors by a *general* mandate in respect of all or any class of information, or by a specific mandate. Additionally, disclosure may be permitted if it is not likely to prejudice the company.

It is, however, important to bear in mind Justice Belinda Ang's observations in Kwee Seng Chio Peter v Biogenics Sdn Bhd (2003) that if a nominee acts merely for another without exercise of his own discretion or volition, in utter disregard for his duties as a director of the company, then he must be bound by notice which the other person, for whom he acts, has of the nature of the transaction. Thus, nominee directors cannot avail themselves to the defence that they were merely puppets on strings.

Where a director acts ostensibly in the interests of a third party or his interests as a shareholder, but such interests coincide with the interests of the company, he would not be in breach of his fiduciary duty towards the company as the law does not prohibit the director from taking into account the interests of a third party or his own interests as a shareholder so long as, ultimately, he acts in the interests of the company as a whole.

It would appear that if the director genuinely believes that he is acting in the interests of the company as a whole, although he might be motivated to act by reason of the consideration of a third party's or his own interest as a shareholder, then the test will rest on the determination of what is the main or actuating motivation. If it is the interests of the company, then the director is not in breach of his fiduciary duty.

8. CONFLICTS OF INTEREST

8.1. Introduction to Conflicts of Interest

It is a well-established principle of law that a person owing a fiduciary duty to another shall not be allowed to place himself in a position where he has, or can have, a personal interest conflicting, or which may possibly conflict, with this duty (Chua Boon Chin v JM McCormack (1979)).

It should be noted that, consistent with the general fiduciary duty of a director to act in good faith and in the interests of the company, such director must also ensure that he is not faced with a situation where there is an actual, or a real and sensible possibility, of a conflict arising between his personal interest and his duty as director. This principle extends also to conflict of interests between the directors' duties and the interests of third parties. This rule, which has been described as 'inflexible', was stated in Furs Ltd v Tomkies (1935) to be based not on morality but on expediency.

The application of this principle gives rise to the prohibition against a person from making or acquiring a personal profit, gain or benefit from his position as a fiduciary.

The remedies available to the company where a director has breached his fiduciary duty by reason of a conflict of interests situation are:

(a) the granting of an injunction by the court to restrain the director from pursuing his personal interests or the interests of a third person;

(b) the accounting of the profits or gains that the director had in fact received, regardless of whether the company had suffered a loss;

(c) the recovery of any property received and retained by the director as a result of the breach;

(d) the recovery of compensation for any loss suffered by the company by reason of the director preferring his own personal interests or the interests of a third party; and/or

(e) the rescission of the transaction that is tainted with the director's breach and the restoration of the parties to their original positions as if the transaction never took place, provided that such transaction has not been completed and is capable of being reversed.

8.2. Dealings Directly Between the Director and the Company

This invariably leads to a conflict of interests. This is so even where the transaction is fair to the company on terms and price, the director concerned has acted in good faith and that the transaction is in the interest of the company. The point here is that, if the transaction involves a sale of property or goods by the director to the company, there is a real and sensible possibility of conflict of interests, as the company would wish to secure the lowest price possible from the director and the director would wish to extract the highest price possible from the company. As such, the company can seek rescission of the contract if the market value of the asset or transaction declines. In addition, the company can seek disgorgement of any profits the director receives from the transaction.

Another example is where the directors exercise their powers to allot shares to themselves. If the shares are allotted at a price below the market price of the shares, then the directors are liable to account for the price difference as a personal profit gained by them as a result of the exercise of their powers. If such shares were sold by the directors at a price higher than the market price of the shares at the date of allotment, the company can recover the full price difference from the directors.

To illustrate the above, in the local case of Kumagai-Zenecon-Construction Pte Ltd v Low Hua Kin (2000), the director of the plaintiff company caused the company to purchase shares in another company so that he could become a director of the latter company in the future. A bank loan was obtained to finance the purchase. When the value of the shares declined, the company was forced to sell the shares at a loss in order to repay the bank. The court held the director liable for his breach of fiduciary duty to act in the best interests of the company and ordered him to compensate the company.

Notwithstanding the foregoing, a director can enter into transactions with the company provided that he makes sufficient disclosure of any conflict of interests, and obtains the relevant approval from the company. In fact, under the Act (S. 156), a director must, as soon as practicable after the relevant facts have come to his knowledge, declare to the company's board the nature of his interest in a transaction or proposed transaction. In Dayco Products Singapore Pte Ltd (in liquidation) v Ong Cheng Aik (2004), Justice Belinda Ang took the position that a failure to adequately disclose will render a director accountable to the company for profits made from the transaction. Justice Ang went on to elaborate that the law requires disclosure to a fully independent board under S. 156 of the Act, or the shareholders under general law; mere knowledge of the conflict of interests and acquiescence by the board and/or shareholders is insufficient and not disclosure. This should, however, be contrasted against the recent decision of Justice Lai Siu Chiu in Maxz Universal Development Group Pte Ltd v Lian Hwee Choo Phebe (2010). There, Justice Lai preferred the view of the New South Wales Court of Appeal in Woolworths Ltd v Kelly (1991) and held that where directors of a company know of another director's interest in a particular transaction, failure to make formal disclosure will not render that director liable for breach of fiduciary duties. Justice Lai distinguished Dayco Products Singapore Pte Ltd (in liquidation) v Ong Cheng Aik (2004) on the ground that it was not a case where there was in fact informal disclosure to the board of directors. Thus, whatever the exact position of law, there must be some form of disclosure, whether formal or informal.

8.3. Dealings Between the Company and a Third Party Associated With Its Director

The test is whether, on the facts, there exists a real and sensible possibility of a conflict arising in the mind of a reasonable man looking at the circumstances. This is an objective test. Hence, if the circumstances are such that a reasonable man would not consider there to be a real and sensible possibility of conflict arising, any dealings between the company and a third party who is an associate of the director would not render the director liable for a breach of his fiduciary duty.

In most cases, the issue is determined by considering whether the director may, whether directly or indirectly, gain some form of pecuniary benefit from the transaction. There are, however, also some situations where the director may secure non-pecuniary interests that are incompatible with his duties as a director of the company and the interests of the company.

S. 156 of the Act provides that a director who has a direct or indirect interest in a contract with the company must disclose this interest at a meeting of directors as soon as practicable. Failure to make such disclosure would render the contract voidable at the instance of the company and expose the director to criminal sanctions. This provision does not apply where the director is merely a member or creditor of the company who is entering into a contract with the director's company. However, a disclosure to the board only means that no criminal offence is committed, but civil liability remains; it does not absolve the director of his fiduciary duty not to put himself in a position where there is a real and sensible possibility that his personal interest might conflict with that of the company without full disclosure to the members.

Under S. 156, the following must be disclosed:

(a) the nature of a director's interest (whether direct or indirect, including an interest of a family member) in any contract or proposed contract with the company;

(b) the nature, character and extent of any conflict that might arise by virtue of a director holding any office; and

(c) the nature, character and extent of any conflict that might arise by virtue of a director owning any property.

The CA Amendments revised S. 156 to allow a director to send a written notice to the company disclosing any conflict of interests as an alternative to declaring such interest at a board meeting. Such notice shall be given as soon as practicable after the date on which the director became a director, or the date on which the director became directly or indirectly interested in the transaction with the company, as the case may be. These provisions will come into force in Q1 2016 and also extend to CEOs of a company.

In Golden Village Multiplex Pte Ltd v Phoon Chiong Kit (2006), a director was found to have acted in conflict of his duties by siding with one of his three companies against the others in which he was also a director. Justice Lai Siu Chiu stated in no uncertain terms that where a director of a company was also a director of other companies within a group, each company remained a separate legal entity to whom the director owed duties and was not entitled to sacrifice its interest. Justice Lai took the position that the director should have refrained from acting as he was not entitled to subordinate the interests of one for the other.

8.4. Dealings Between the Director and the Shareholders

As a general rule, the fiduciary duties of directors are owed to the company and not the shareholders. However, in certain circumstances, the directors may directly assume ad hoc fiduciary duties in favour of shareholders; for example, where the shareholders depend on the directors for information and advice, or where there exists a relationship of confidence. Where nominee directors can properly represent the interests of a particular section of shareholders, then it may be more readily inferred that such directors owe some fiduciary duties directly to such shareholders.

Similarly, directors of wholly owned subsidiaries may owe fiduciary duties directly to the holding company. That said, it should be noted that the foregoing is in addition to, and not in derogation of, the duties owed by a director to the company. A director can still fall foul of the "no conflict rule" *vis-à-vis* his status as a director of a subsidiary (W&P Piling Pte Ltd (in liquidation) v Chew Yin What and others (2007) and Townsing Henry George v Jenton Overseas Investment Pte Ltd (2007)).

8.5. Business Opportunities of the Company

In general, there is no duty upon a director to refrain from engaging, for his own benefit, in the same kind of business as that carried on by the company provided:

(a) there is no express restraint-of-trade clause if there is an employment contract between the director and the company;

(b) there is no unauthorised use or disclosure of the company's confidential information;

(c) there is no improper use of the company's assets and property; and

(d) there is no breach of the director's fiduciary duty to act in good faith and in the interests of the company and his fiduciary and statutory duty to act with reasonable diligence.

The general rule regarding business opportunities available or under consideration by the company is that the directors are not free to divert or destroy such business opportunities without the proper authority of the company. This obligation persists even after the director has resigned, at least where his resignation was prompted or influenced by the desire to obtain the opportunity for himself.

As an illustration, in the case of Cook v Deeks (1916), two directors (who were also the majority shareholders of the company) had negotiated for a contract on behalf of the company. Some disagreement arose between them and the other directors of the company and, consequently, the two directors formed another company, and caused the contract to be given to the new company that they had formed. Naturally, the other directors in the company were unhappy and took action against the two directors and the new company for a declaration that they were trustees for the company of the benefit of the contract. The two directors, to pre-empt the action, caused a meeting to be held, and they, being the majority shareholders caused the company to pass a resolution that it had no interest in the contract.

The court held that the two directors were in breach of their fiduciary duties to the company and they therefore held the contract given to the new company for the benefit of the company. As the benefit of the contract belonged to the company, the resolution was not effective to deprive the company of its right to the contract.

The rule also applies to business opportunities which the company might reasonably be expected to be interested in given its present field of business activities.

To illustrate the point, in Cranleigh Precision Engineering Ltd v Bryant (1965), the director of a company which manufactured swimming pools made an invention for the construction of walls for swimming pools. This invention was an infringement of another invention that was patented. The director did not disclose the existence of this patented invention to the other directors. The director resigned and joined another company in which his wife and son were directors. He then obtained an assignment of the patented invention and used the company he had joined to manufacture swimming pools using the patented invention and his own invention.

The court held that the director was in breach of his fiduciary duty by concealing the existence of the rival patented invention from the company. He had also violated the law of confidence by making use of the information for his benefit and the benefit of the company he had joined. Accordingly, the director and the new company held the director's own invention and the patented invention that he had acquired for the benefit of the company.

In the local case of Chew Kong Huat v Ricwil (Singapore) Pte Ltd (2000), a husband and wife who were both directors of Ricwil caused the cancellation of eight contracts between Ricwil and its customers. They then diverted the contracts to another company in which they were interested. By preferring the interests of another company over Ricwil, they failed to act in the interests of Ricwil and had to pay damages to Ricwil.

It makes no difference that the company itself was unable to exploit the business opportunity. If the director then acquired the investment for himself, he would have breached his duty towards the company. In Regal (Hastings) Ltd v Gulliver (1942), the English Court held that a director in such a case could have obtained an assent from the shareholders to take up any business opportunity which the company has passed up, and failing which, he has no choice but to let the opportunity pass.

In another case, the director of a company in Industrial Development Consultants v Cooley (1972) resigned from his company in order to secure certain contracts which his company wanted. The Gas Board had refused to grant his company the contracts. The director argued that he did not breach any duty because the company could not have gotten the contracts anyway. However, the court held that the director had put himself in a position in which his duty to the company and his self-interest grievously conflicted. Thus, the director had to account for his profit to the company.

The law appears to be strict in that once the court ascertains that there is a real and sensible possibility of conflict, it is the duty of the director to avoid personal involvement. The duty on the director is not merely to avoid taking advantage of the company. The court will not come to a different decision even if the transaction was fair to the company.

Where after a consideration of the business opportunity, the directors reject the business opportunity for the benefit of the company in good faith and as a matter of business judgment, it would appear that the directors may then be free to exploit that business opportunity for their own personal benefit. In Canada, the Supreme Court in Peso Silver Mines Ltd (NPL) v Cropper (1966) allowed a director in such a case to take up the business opportunity which his company had genuinely rejected without the need for disclosure. They permitted this as long as the directors of the company acted honestly in the best interests of the company when rejecting the opportunity. This is a more commercially realistic view.

There is an extremely fine line of distinction whether the directors would be in breach of their fiduciary duties to the company. On the one hand, there are arguments that the fact that the company cannot or does not wish to exploit the business opportunity is irrelevant. On the other hand, it may be said that once the board of directors have rejected the business opportunity available to them as a matter of business judgement, then the company no longer has an interest in that business opportunity and it should then be free for the directors to exploit that business opportunity as there would not be any real and sensible possibility of conflict.

8.6. Directors' Right to Compete

It would appear that there is no blanket prohibition against a director from competing with the company in which he is a director, or that a person cannot be a director of two competing companies. As long as the potential conflict is disclosed to the company and approved, the holding of cross-directorships is not *per se* a breach of fiduciary duty.

The English case of London and Mashonaland Exploration Co Ltd v New Mashonaland Exploration Co Ltd (1891) held that a director will not be in breach of his fiduciary duty merely by competing with the company, or by having an interest in or being a director of a competing company.

It should, however, be noted that such a prohibition may be imposed by implied or express agreement between the company and the director through the use of, for example, restrain-of-trade clauses and the implied obligation to devote full time and attention to the affairs of the company.

It should also be noted that the director should not utilise the property and assets of the company for the benefit of the competing company; disclosure to or utilisation by the competing company of confidential information belonging to the company; or the diversion of business opportunities away to the competing company.

S. 156 of the Act requires directors who hold any office or possessing any property whereby their interests might be in conflict with their duties or interests as director of the company to declare this fact and its nature, character and extent of the conflict in a meeting of directors (see 9.2 below).

8.7. Improper Use of Information

Confidential information cannot be used or disclosed by the recipient without the consent or authorisation of the owner of such information. The obligation of confidentiality arises where the information is of a type not generally known to the public, and it has been disclosed to the recipient in circumstances giving rise to an obligation of confidentiality. Such a duty does not depend on the existence of a fiduciary relationship.

S. 157(2) provides that an officer of the company shall not, at any time, make improper use of any information acquired by virtue of his position as an officer of the company to gain an advantage for himself, whether direct or indirect, or for any other person, or cause detriment to the company.

As discussed earlier, the SC has stated in its Report that there is no need to exhaustively codify directors' duties, given that the Act already contains a statutory statement on directors' duties under S. 157. In addition, ACRA has also published a guidebook for directors. Hence, the SC and MOF have decided to keep the current status quo and will instead continue to monitor the developments in the UK and other jurisdictions.

The CA Amendments has extended S. 157(2) to cover improper use by an officer or agent of a company of his position to gain an advantage for himself or for any other person or to cause detriment to the company. The test under S. 157(2) is whether an individual had obtained an unfair advantage through an abuse of his position. Consequently, it is irrelevant whether it concerns merely information or otherwise.

An officer or agent in breach of this section shall be accountable to the company for any profit made by him or for any damage suffered by the company as a consequence thereof. A criminal penalty is also imposed. As discussed earlier, the MOF agreed with the SC that the criminal liability provisions under S. 157 should be retained as a deterrent and to encourage better governance.

An example of improper use can be seen in Golden Village Multiplex Pte Ltd v Phoon Chiong Kit (2006), where Justice Lai Siu Chiu affirmed that a director's fiduciary duties at common law prohibited him from using confidential information gained from attendance at board meetings to the detriment of the company.

8.8. Steps to Avoid Incurring Personal Liability in a Conflict-of-Interest Situation

The company may, at a general meeting, authorise or ratify any transaction entered into by a director in a situation where his duty was in conflict with his interest in the contract, unless the articles otherwise provides.

There must be full disclosure of both the nature and extent of the conflicting duty or interest to the shareholders before there can be a valid ratification from the shareholders.

It would appear that the director concerned may, as a shareholder, vote in the general meeting, provided that there is no improper dealing with the company's property. Care must be taken, however, to avoid any suggestion that the exercise by the director of his voting rights as a shareholder constitutes a fraud or oppression of the minority, or that it is unfairly prejudicial to the conduct of the company's affairs.

As a general rule, the board of directors cannot consent to a director having an interest in a transaction with the company, even if such director abstains from voting. However, the articles may empower the directors to so consent to a director being interested in a transaction or continue to act as director whilst having a conflict of interest or duty. In such a case, the board of directors must scrutinise the transaction to ensure that it is fair to the company and that the transaction is in the interest of the company as a whole.

Where the interested director is entitled to vote on a transaction that he has an interest in or where there is a conflict, he must still exercise his vote in such a manner that is in the interest of the company as a whole.

S. 156 of the Act requires the directors to declare their interests in any contract or proposed contract with the company to the meeting of directors. S. 156 will also be revised to give directors an option to declare their interest via written notice to the company.

The failure to comply with S. 156 creates a criminal offence punishable with a fine not exceeding $5,000 or imprisonment not exceeding one year.

A contravention of S. 156 may also give sufficient ground for the disqualification of the person to act as director.

The articles may also provide for the disqualification of directors if they fail to declare their interests in contracts with the company.

9. SUBSTANTIAL PROPERTY TRANSACTIONS

9.1. Disposal of the Whole of the Company's Undertaking or Property (S. 160)

S. 160(1) of the Act requires, unless the approval of the company in general meeting has been obtained, that the directors shall not carry into effect any proposals for the disposal of the whole or substantially the whole of the company's undertaking or property, notwithstanding anything in the company's memorandum or articles.

This restricts the directors' powers of management and is primarily designed to ensure that directors do not take advantage of their position to obtain a benefit from the company without the approval of the members and to give the members some say on fundamental issues of the company's affairs that affect their interests as members.

9.2. Repealed Sections

The statutory provisions governing substantial property transactions between a company and a director, or a person connected with the director (previously set out in S. 160A - S. 160D of the Act), were repealed by the Companies Amendment Act (1998).

Various commentators had, from time to time, voiced out the lack of clarity in the wordings of those provisions. The provisions had also given rise to practical difficulties for companies, particularly in the retail and service sectors, because under the requirements of those provisions, a company was required to convene a general meeting each time the company entered into such related party transactions.

It must be noted that, notwithstanding the abolition of those provisions, directors are required under the common law to disclose to shareholders and obtain shareholders' approval before the directors and/or person(s) connected with the directors enter into any transaction with their companies.

This requirement can, however, be satisfied if the company's Articles of Association stipulate clearly that a director is not required to account to the company for any profit or gain pursuant to any contract or transaction entered into between the director (and/or person(s) connected with the director) and the company, subject to due disclosure to the board of directors, and approval of the transaction or contract in question by the board.

9.3. Liquidator's Right to Recover in Certain Sales to or by the Company (S. 331)

Under S. 331(1) of the Act, if there has been a sale, for cash consideration (i.e., consideration payable otherwise than by the issue of shares in the company), to the company by its director or by a company of which its director was also a director of the first-mentioned company of any property, business or undertaking within two years of the commencement of the winding up of the first-mentioned company, the liquidator is empowered to recover any payment made by the first-mentioned company that exceeded the value of the property, business or undertaking at the time of acquisition.

Similarly, under S. 331(2) of the Act, if there has been a purchase, for cash consideration, from the company by its director or by a company of which its director was also a director of the first-mentioned company of any property, business or undertaking within two years of the commencement of the winding up of the first-mentioned company, the liquidator is empowered to recover the value of the property, business or undertaking in excess of the cash consideration received by the first-mentioned company at the time of sale.

The underlying policy behind S. 331 of the Act is essentially to prevent diminution in the company's net assets and to prevent any creditor of the company from gaining an unfair advantage over the other creditors.

9.4. Disclosure of Sale to Interested Persons Under the Listing Manual

Companies listed on the SGX-ST are required to observe the requirements under Chapter 9 of the SGX-ST Listing Manual in respect of interested person transactions between an interested person, namely: (i) a director; (ii) the CEO; (iii) a controlling shareholder; or (iv) an associate of any such director, CEO or controlling shareholder, and an entity at risk, namely: (i) the company in question; (ii) its subsidiary; or (iii) its associated company, provided that the listed group or the listed group and its interested person(s) has control over the associated company. The objective is to guard against the risk that interested persons could influence the listed company, its subsidiaries or associated companies to enter into transactions with interested persons that may adversely affect the interests of the listed company and its shareholders.

A company listed on the SGX-ST is required under Rule 910(1) of the Listing Manual to announce a sale or proposed sale of any units of its local property projects or those of its entity at risk to an interested person or a relative of a director, CEO or controlling shareholder within two weeks of the sale or proposed sale. This is regardless of whether the sale or proposed sale is required to be announced under Rule 905 of the Listing Manual (discussed below in 10.4). If the sale or proposed sale involves any units of its nonlocal property projects or those of its entity at risk to its interested person, the listed company is required to comply with Rule 905 (discussed below in 10.4).

Several safeguards are included under Chapter 9 of the Listing Manual to specifically prevent unfair dealing of a company's property projects. In particular, Rule 912 of the Listing Manual stipulates that when deciding whether to offer any sale of units in its property projects to a listed company's interested persons or a relative of a director, CEO or controlling shareholder, the listed company's board of directors have to be satisfied that the terms of the sale are not prejudicial to the interests of the company and its minority shareholders. In addition, Rule 912 of the Listing Manual further states that the audit committee must review and approve the sale and satisfy itself that the number and terms of the sale are fair and reasonable and are not prejudicial to the interest of the listed company and its minority shareholders. Rule 913 of the Listing Manual also stipulates that where a sale or proposed sale to an interested person requires shareholder approval, the listed company must obtain the approval within six weeks of the date of the sale or proposed sale. Finally, Rule 914 of the Listing Manual stipulates that an interested person or his nominee must abstain from voting on all resolutions approving the sale or proposed sale to the interested persons.

Since the Audit Committee of a listed company is required to review and approve of any sale relating to a company's property project, a short introduction of the Audit Committee's functions will be useful to help us appreciate its importance. In essence, the Audit Committee plays an important role in ensuring the accurate and transparent disclosure of a company's financial situation and controls. Guideline 12.1 of the Governance Code recommends the establishment of an Audit Committee, which should comprise at least three directors, the majority of whom, including the Audit Committee's Chairman, should be independent. All the members of the Audit Committee should be nonexecutive directors. Under Guideline 12.2 of the Governance Code, the board should also ensure that members of the Audit Committee are appropriately qualified to discharge their responsibilities. The importance of the Audit Committee is highlighted in the following scenario. In January 2013, Kingsmen Creatives Ltd., a listed company, announced that two of its subsidiaries are believed to have committed fraud, which was discovered only when its Audit Committee noted misappropriation of funds in its subsidiary between 2009 and 2011. This shows that the Audit Committee is indeed a useful tool that is used in practice to ensure that the company's finances are in check.

Finally, it is pertinent to note Rule 923 of the Listing Manual, which expressly states that the SGX-ST will not entertain any application for a waiver of the provisions of Chapter 9 of the Listing Manual relating to interested-person transactions.

10. OTHER MATTERS RELATED TO FIDUCIARY DUTIES AND CONFLICT OF INTERESTS

10.1. Loans to Directors

Part of the duty of directors to act in good faith and in the interests of the company is to ensure that the company's resources are used solely for the benefit of the company as a whole. The application of this results in directors being in breach if they make a secret profit for themselves from the property, assets, confidential information or business opportunities of the company that they represent.

Loans to directors may perhaps be classified within this rule – loans to directors would give rise to a real and sensible possibility of a conflict of interest and duty. The director would benefit from the loan transaction, which is at cross purposes with the interests of the company, even if there is an agreement for the loan to be repaid with interest because there is an opportunity cost being borne by the company in relation to the alternative deployment of the amount represented by the loan.

S. 162(1) of the Act provides that loans by a company to its directors or to directors of related corporations are in general prohibited. S. 162(6) further provides that a company may not make a loan to a director's spouse or children (whether adopted or natural). If a loan is made in contravention of S. 162 of the Act, the directors who authorised the transaction may be convicted of an offence under S. 162(4) of the Act. Furthermore, since the directors who authorised the transaction would have breached their fiduciary duties in contravening the law, they may be required to indemnify the company for losses incurred due to their breach of duty. It is also specifically provided that if the company does not give approval for a loan where approval is required pursuant to S. 162(2) of the Act, the directors who authorised the transaction will be jointly and severally liable to indemnify the company against any loss. However, the director to whom the loan is made does not contravene this section or commit an offence. If he knew or ought to have known that the loan was made in breach of S. 162, he will probably hold it on constructive trust for the company (i.e., he will have to return it).

S. 163(1) extends the prohibition by preventing directors from making loans to companies which they control. The section provides that a company cannot make a loan to another company if the directors of the lending company have an interest in 20% or more of the shares of the borrowing company. Pursuant to S. 163(2)(a), this prohibition also applies where the borrowing company is incorporated outside of Singapore. Under S. 7 of the Act, a person is deemed to have an "interest in shares" that a company has or is deemed to have if he has a controlling interest in the company or the company is, or its directors are accustomed or under an obligation to act in accordance with the directions, instructions or wishes of that person. Under S. 163(5) of the Act, an interest in shares of the director's spouse, children (whether adopted or natural) is to be treated as the director's interest. It is pertinent to highlight that the SC has received industry feedback that S. 163 has caused problems in practice for companies incorporated in Singapore, particularly in joint venture situations. However, after consulting with various focus groups, the SC has decided to retain the share-interest threshold of 20% in S. 163.

This prohibition also extends to the company standing as guarantor or providing collateral to secure loans extended to its directors or any person or corporation connected with such directors by third parties. It should be noted that these two sections do not prevent the recovery of any loan or the enforcement of any security by a third party under S. 162(5) and S. 163(6) of the Act. However, if the third party was aware that the directors were acting beyond their authority or in breach of their fiduciary duties, it may be that the company could set aside the guarantee or security.

The prohibition under S. 162 does not apply in limited circumstances which include, *inter alia*, a loan to a director for expenses he is expected to incur in the performance of his duties, loans to directors by companies not incorporated in Singapore and employee loan schemes.

In addition, the prohibition under S. 163 does not apply, *inter alia*, to anything done by a company where the other company is its subsidiary, holding company or a subsidiary of its holding company.

Under the CA Amendments, the restrictions in S. 162 and S. 163 of the Act will be extended to cover quasi-loans, credit transactions and related arrangements. Given that many new types of financial instruments and arrangements have developed over time, the SC noted that Singapore should update its regulatory regime to keep pace with the changing business environment and to remain on par with leading jurisdictions such as the UK and Australia. The MOF agreed with the views of the SC on this matter.

The CA Amendments introduced an exception to S. 163 of the Act to allow a transaction if prior shareholders' approval in a general meeting is obtained. Directors and their family members who are interested in the transaction must abstain from voting unless all the shareholders of the company vote to approve the transaction.

Apart from the foregoing, two general exceptions to S. 162 and S. 163 will also be implemented. The new S. 163A and S. 163B allow a company to provide a director with a loan to meet expenditure incurred under the following circumstances:

(a) in defending himself against any criminal or civil proceedings in connection with any alleged negligence, default, breach of duty or breach of trust by him in relation to the company;

(b) in connection with any application for relief;

(c) in defending himself against an investigation by a regulatory authority; or

(d) in defending himself against any action to be taken by a regulatory authority.

The above exceptions will only apply to loans and not quasi-loans, credit transactions or related arrangements. These changes are expected to come into force in Q1 2016.

The SGX-ST Listing Manual also provides for the disclosure (see 10.4(a) below) of an interested person transaction which includes, *inter alia*, the provision or receipt of financial assistance between a listed company or its subsidiaries, and a director or his associate. An associate is defined in the Listing Manual as, *inter alia*, a director's immediate family and a company in which he and his family together have an interest of 30% or more.

10.2. Obligations to Disclose

The reason for the imposition of disclosure obligations on directors is to provide a form of safeguard against improper transactions by directors and against unfounded suspicions of such transactions.

Accordingly, the Act imposes requirements on directors to make public certain types of information concerning themselves. Some of these requirements have already been referred to earlier; for example, the obligation to declare interests in contracts, and the existence of any conflicts by reason of office or holding of property. In the case of a public-listed company, the SGX-ST Listing Manual also requires a director to declare to the company (which in turn is required to release this disclosure to the public) such personal information as required in Appendix 7.4.1 or 7.4.2 relating to his appointment and cessation respectively and Appendix 7.2 relating to the disclosure of managers in the listed company or any of its principal subsidiaries who are related to him.

The following are additional disclosure obligations of directors:

(a) **Shareholdings and Other Interests in the Company**

A director is under a duty to give notice in writing to the company, of particulars concerning his holding of and interests in the shares of the company and any other related corporation (S. 165(1)(a) and (b) and S. 164).

In addition to shares, the disclosure of particulars relating to any debentures, participatory interests, rights, options and contracts in respect of the acquisition or disposal of shares or a right to call for or make delivery of shares of the company and any related corporation as well as any change thereto is also required.

Notwithstanding the fact that the UK, Hong Kong and Australia have done away with the register of directors' shareholdings and other interests specified under S. 164(1), the SC has recommended that the status quo be maintained in the interests of transparency and disclosure. The information about directors' shareholdings would impact a director's position on the board if there was a conflict of interest. Also, a minority investor may wish to have information about such interests. In addition, the register enables a private company to be aware of its directors' shareholdings, and enables the parent company of a wholly owned subsidiary to know similar details about its subsidiary. The register would also be useful for shareholders who may require such information when making decisions about the company. The MOF shared the views of the SC that the register of directors' shareholdings remains relevant and should be retained.

The CA Amendments to S. 164 will also extend the current provisions to CEOs of a company. These changes will come into effect in Q1 2016.

(b) **Personal Particulars (S. 165(1)(c) and S. 173(2)(b))**

The director is under a duty to give notice, in writing, to the company of particulars concerning his present full name, former name, usual residential address, nationality, business occupation and his identity card or passport number.

Under the CA Amendments, a director may elect to provide an alternate address instead of his residential address. These changes will take effect in Q1 2016.

(c) **Directorships in Public Companies (S. 156(4))**

It is a practice in Singapore for directors to inform his company in writing of any other directorships held by him. This serves to put the company on notice of the director's competing directorship in the event the company is involved in a future transaction in which the director is deemed to be interested in by virtue of his directorship in another company. As mentioned earlier, the CA Amendments to S. 156 will give the director the option of declaring his interest at a meeting to the other directors or send a written notice to the company setting out the nature, character and extent of the conflict. These changes will come into effect in Q1 2016.

Guideline 4.4 of the Governance Code states that when a director has multiple board representations, he or she must ensure that sufficient time and attention is given to the affairs of each company. The Committee should decide if a director is able to and has been adequately carrying out his duties, taking into consideration the director's number of listed company board representations and other principal commitments. The board of directors of a company should also determine and disclose the maximum number of listed company board representations which any director may hold in the annual report. Presumably, failure to devote adequate time and attention to a company may be taken into account during a re-election of the director.

(d) **Emoluments (S. 164A)**

The shareholders (either representing at least 10% in terms of numbers or 5% in terms of nominal value of issued share capital) are entitled to receive, by notice in writing to the company, an audited statement setting out the total amount of emoluments and other benefits paid to or received by each director of the company and of the subsidiary.

In respect of the disclosures under paragraphs (a) to (d) above, the company is obliged to send a copy of the notice to every other director within seven days of receipt by the company pursuant to S. 165(3) of the Act. If the company is listed on the SGX-ST, the director must similarly notify the SGX-ST, which may publish any information received by it.

(e) **Other Payments to Directors (S. 168)**

Under S. 168(1) of the Act, any payment by a company to its director for loss of office or retirement from office must be disclosed to the shareholders and approved by them at a general meeting, unless such payment is a *bona fide* payment by way of damages for any breach of contract, is a *bona fide* payment by way of pension or lump sum payment for past services, or is a payment to a director pursuant to an agreement between the director and the company before he became a director as consideration for him agreeing to serve the company as a director, as stipulated under S. 168(5) of the Act.

As discussed earlier, the requirement in S. 168 for shareholders' approval for the payment of compensation to directors for loss of office continues to be retained under the CA Amendments. However, a new exception has also been introduced to obviate the need for shareholders' approval under the circumstances elaborated in paragraph 6.5.

Similarly, under S. 168(1) of the Act, any payment to any director of a company in connection with the transfer of the whole or any part of the undertaking or property of the company must be disclosed to the shareholders and approved by them in general meeting.

According to S. 168(3) of the Act, any payment received by a director in contravention of this section shall be held by him on trust for the company.

(f) **Disclosure in the Annual Report**

Guideline 4.7 of the Governance Code also provides that directors disclose key information about themselves in the annual report. Examples of such information include academic and professional qualifications, shareholdings in the company and its related corporations, board committees served on, date of first appointment as a director, date of last re-appointment as a director, directorships or chairmanships both present and those held over the preceding three years in other listed companies and other principal commitments.

10.3. Disclosure Requirements for IPOs

(a) Background

The prospectus regime under the SFA prescribes civil and criminal penalties for the failure to disclosure material facts, or the disclosure of misleading information.

S. 243(1) of the SFA requires a prospectus to contain: (i) all the information that investors and their professional advisors would reasonably require to make an informed assessment of the matters relating to the securities and the issuer specified in S. 243(3); and (ii) the matters prescribed by the MAS. Consistent with the practice in the UK and Hong Kong, the reasonable investor test, as well as detailed checklists promulgated under the SFA, are applied when determining what information should be disclosed.

Under S. 243(4) of the SFA, in deciding what information to include in the prospectus, the company should have regard to the nature of the shares, the matters that potential investors may reasonably be expected to know and the matters that professional advisors of such investors would reasonably be expected to know.

S. 243(2) of the SFA sets the boundaries on the amount of disclosure required of an issuer. S. 243(2)(a) of the SFA provides that the prospectus should contain such information only to the extent to which it is reasonable for investors and their professional advisers to expect to find in the prospectus. In deciding what investors and their professional advisors can reasonably expect to find, persuasive cases in Australia such as <u>Pancontinental Mining v Goldfields Ltd (1995)</u> and <u>Fraser v NRMA Holdings Ltd (1995)</u> have determined that industry norms, relevance and reliability of information were factors to be considered. In addition, S. 243(2)(b) of the SFA provides that the prospectus should contain such information only to the extent that a 'person' whose knowledge is relevant actually knows the information, or ought reasonably to have obtained the information by making enquiries. S. 243(5) of the SFA further provides that such 'person' includes, *inter alia*, a director of the issuer. Hence a director can be made liable for misleading statements contained in a prospectus.

(b) Common Law Liability

Before the provisions of the SFA are explained, it is pertinent to note that the common law provides remedies for misstatements contained in a prospectus under the tort of deceit.

An investor who suffers loss because of a deliberate misrepresentation or omission may recover damages for deceit, which requires proof of fraud and this can be shown if the false representation has been made knowingly, or without belief in its truth, or recklessly, without caring whether it be true or false.

The case of <u>Hedley Byrne v Hedler & Partners (1964)</u> decided that tortious liability for misstatements can be established if a special relationship exists between a company, or its directors, and the investors relying on the prospectus. If fraud can be shown, damages are awarded to fully compensate the person for all losses caused by the misrepresentation.

Liability for misrepresentation can only attach to a party to the contract. Thus, in the IPO situation, the issuer will be liable to investors if the statement was made or attributable to the issuer. According to the court in <u>De Cruz v Guangzhou Yuzhitong (2003)</u>, directors who authorise the issue of the prospectus may also be liable at common law for the tort of negligence where their involvement was 'total'.

(c) Criminal Liability

S. 253(1) of the SFA prescribes criminal penalties for misstatements contained in a prospectus for an offer of shares to the public. Misstatements include: (i) the provision of false and misleading information; (ii) an omission to state information required to be included under S. 243 of the SFA; or (iii) an omission to state a new circumstance that has arisen after the lodgement of the prospectus with the MAS and would have been required to be included in it under S. 243 of the SFA.

Under S. 253(2) of the SFA, a person is deemed to have made a false and misleading statement about a future matter if there are no reasonable grounds for making the statement. However, S. 253(3) of the SFA clearly stipulates that a false and misleading statement, or the omission to state any information or new circumstance, will not be taken to have contravened S. 253(1) if it is not materially adverse from the point of view of an investor.

Under S. 253(1) of the SFA, directors of the issuer who breach S. 253 of the SFA can be liable on conviction to a fine not exceeding $150,000 or to imprisonment of not more than two years, or both.

(d) **Civil Liability**

The civil liability provisions in S. 254 of the SFA largely mirror those in S. 253 of the SFA, except for the absence in S. 254 of the section to the effect that a false and misleading statement, or the omission to state any information or new circumstance, will not be taken to have contravened this section if it is not materially adverse from the point of view of an investor.

Under S. 254(1) of the SFA, directors of the issuer who breach S. 254 of the SFA are liable to compensate any person who suffers loss or damage as a result of the false and misleading statement in or omission from the prospectus.

(e) **Defences**

A director has several defences available under S. 255 of the SFA for a breach of the foregoing sections. Firstly, a director will not be liable for misstatements in a prospectus if he had made all reasonable enquiries and after doing so, believed on reasonable grounds that the statement was not false or misleading, or that there was no omission (S. 255(1) and (2) of the SFA).

Secondly, a director will not be liable for misstatements in a prospectus if he reasonably relied on information given to him by someone other than his employee or agent (S. 255(3)(b) of the SFA).

Thirdly, a proposed director will not be liable for misstatements in a prospectus if he publicly withdraws his consent from being named in the prospectus (S. 255(5) of the SFA).

Finally, a director will not be liable if he is unaware of new circumstances that had arisen since the lodgement of the prospectus with the MAS (S. 255(6) of the SFA).

In addition to the above, a director charged under the criminal section can avoid liability by showing that the misstatement is not materially adverse from the point of view of the investor (S. 253(3) of the SFA).

(f) **Due Diligence Committees**

Although due diligence committees are not compulsory in Singapore, especially when the issue size is small, the market practice is that directors' due diligence meetings or verification exercises are held in which the board of directors of the issuer will review the prospectus as a whole for any factual inaccuracies. Ongoing due diligence is also required as the Act prescribes penalties for the nondisclosure of new circumstances which arise after lodgement of the prospectus.

10.4. Disclosure Requirements Under the SGX-ST

(a) Interested Person Transactions

Chapter 9 of the SGX-ST Listing Manual imposes certain requirements on listed companies in relation to interested-person transactions. Under Rule 905 of the Listing Manual, a company is required to make an immediate announcement of any interested-person transaction if the value of the transaction, or the aggregate value of all transactions entered into with the same interested person during the same financial year is equal to or above 3% of the latest audited net tangible assets of the group.

Under Rule 906 of the Listing Manual, the company must obtain shareholders' approval if the value of the transaction or the aggregate value of all transactions entered into with the same interested person during the same financial year is equal to or above 5% of the latest audited net tangible assets of the group.

The requirements of Chapter 9 do not apply to transactions below $100,000. In addition, the issuer must disclose the aggregate value of interested-person transactions entered into during the financial year under review and the names of the interested persons in its annual report under Rule 907 of the Listing Manual.

(b) Compliance with Listing Rules

Due to the contractual nature of the listing rules, and privity (parties to) of contract between the listed company and the SGX-ST, the SGX-ST probably does not have direct recourse against persons such as a director for non-compliance with the Listing Manual, but only against the listed company itself. However, in practice, the rulings of the SGX-ST are adhered to by persons that are associated with the listed company, usually the directors.

It was held in <u>Dickson Trading (S) Pte Ltd v Transmarco Ltd (1989)</u> that it was 'common ground' between the contracting parties that a sale of shares in a subsidiary by a listed company was subject to the approval of the company's shareholders as required by the Listing Manual. The listing rules may thus become terms that are *incorporated* into contracts entered into by parties not directly privy to those rules.

A failure to comply with the Listing Manual may lead SGX-ST to discipline the listed company, but not expressly a director. Under Rule 1305 of the Listing Manual, SGX-ST may delist a company if an issuer is unable or unwilling to comply with, or contravenes a listing rule. However, unlike some other exchanges elsewhere, it does not have the power to fine listed companies that fail to comply with the listing rules nor does it have any real formal sanctions against third parties, such as directors. Nonetheless, in recent times, the SGX-ST seems to be taking on a more involved role in subjecting directors to some form of regulatory action. Pursuant to the amendments to Rule 720 of the Listing Manual on 29 September 2011, the SGX-ST now has the right to publicly censure or object to the appointment of key executive officers or directors. However, the reality is that further improvements to corporate governance is likely to require some form of recognition that the SGX-ST rules are more than merely contractual in nature.

Nonetheless, recent developments in the UK may provide some indication on the course the SGX-ST may take in the future with regards to errant directors. The Financial Services Authority ("**FSA**") in the UK considered whether it should be given the power to disqualify a director for a serious breach of the listing rules in *FSA's Review of the Listing Regime, CP 203, October 2003*. Presently, the FSA has the power to fine both directors and companies.

(c) Continuing Obligations

Chapter 7 of the Listing Manual sets out continuing disclosure requirements for companies listed on the SGX-ST, in particular information relating to changes in capital, interested person transactions, acquisitions and realisations, takeovers, circulars and annual reports. Rule 703(1) of the Listing Manual provides that a listed company must announce any information known to it concerning it or any of its subsidiaries or associated companies which is: (a) necessary to avoid the establishment of a false market in the listed company's securities; or (b) which would be likely to materially affect the price or value of its securities.

However, Rule 703(3) of the Listing Manual provides that a company is not required to disclose the information stipulated in Rule 703(1) if: (a) a reasonable person would not expect the information to be disclosed; (b) the information is confidential; and (c) the information concerns an incomplete proposal or negotiation, comprises matters of supposition or is insufficiently definite to warrant disclosure, is generated for the internal management purposes of the entity or is a trade secret.

An intentional or reckless breach of Rule 703 of the Listing Manual constitutes an offence under S. 203 of the SFA, which requires a listed company to notify the SGX-ST of such information as is required to be disclosed by the SGX-ST under its listing rules or any of its other requirements. According to S. 204 of the SFA, any person who is guilty of such an offence shall be liable on conviction to a fine not exceeding $250,000 or to imprisonment for a term not exceeding seven years or both.

In Madhavan Peter v Public Prosecutor and other appeals (2012), the Singapore High Court distinguished between two different regimes of materiality as applied to offences relating to nondisclosure under Rule 703(1)(b) of the Listing Manual read with S. 203 of the SFA and offences relating to insider trading under S. 218 read with S. 216 of the SFA. According to Chief Justice Chan Sek Keong, the word "material" in Rule 703(1)(b) of the Listing Manual refers to information that is likely to effect a significant change in the price or value of an issuer's securities (i.e., materially price sensitive information). On the other hand, the concept of materiality for the offence of insider trading under S. 218 read with S. 216 of the SFA refers to information which would, or would be likely to, influence persons who commonly invest in securities in deciding whether to subscribe for, buy or sell the securities concerned (i.e., trade-sensitive information). Hence, Chief Justice Chan held that Rule 703(1)(b) of the Listing Manual read with S. 203 of the SFA has a narrower scope of operation than S. 218 read with S. 216 of the SFA. This means that while directors may not be required to disclose trade-sensitive information, they have an obligation to disclose information that is materially price sensitive.

In situations where the likely market impact of information is unclear and a board is uncertain as to whether disclosure of the information is required, it will be prudent for a board to obtain independent legal advice on the question of whether disclosure should be made so as to refute any potential allegations of recklessness on its part. It is not unreasonable for directors to rely on such independent legal advice. Chief Justice Chan held that a board is not under any obligation to question the legal advice that it receives unless such advice is manifestly absurd, irrational or wrong. But, this does not mean that boards can simply refer the matter to lawyers and wash their hands of the matter. The board is required to exercise independent judgment at every step of the way in determining: (i) whether disclosure is required having regard to the nature of the information and the circumstances and facts of the particular case; (ii) whether legal advice should be taken; (iii) whether the advice that is obtained is manifestly absurd, irrational or wrong and should be disregarded and whether a second opinion should be sought; and (iv) whether disclosure should be made having regard to any legal advice that has been sought and obtained and in all the circumstances of the particular case.

11. DUTY OF CARE, SKILL AND DILIGENCE

11.1. Introduction to the Duty of Care, Skill and Diligence

The duty of care, skill and diligence may be imposed on directors through: (a) contract; (b) fiduciary duty; (c) the common law tort of negligence; or (d) statute.

11.2. Contract

It is becoming more common for executive directors to enter into contracts of employment with the company. In such a contract, there may be express or implied terms that the employee will exercise the care and skill to be expected of a person who occupies the position in question. Such contracts may also require the employee to devote full time and attention to his employment.

11.3. Fiduciary Duty

Directors owe a fiduciary duty to the company to exercise proper care and skill in the discharge of their function as directors. In the proper discharge of fiduciary duty to the company, the directors are also required to act with due diligence to attend to the affairs of the company that concerns the board.

11.4. The Common Law Tort of Negligence

Where a person owes a duty to another and there is a breach of that duty resulting in loss or damage to be suffered by this other person, then the person owing that duty is liable to compensate the victim for the loss or damage suffered. A duty arises when it is reasonably foreseeable that the other person would suffer loss or damage by reason of an act or omission of the first person.

At present, there does not appear to be any case law that has stated that the common tort law duty of care would apply to directors. Suffice to say that in most cases, the application of the common law duty of care is not necessary, as the existence of the director's fiduciary duty towards the company would be sufficient to establish liability. However, in theory, there is no reason why this common law duty of care should not apply to directors who, in many instances, are required to advise the company and to act on its behalf. It would be reasonably foreseeable that the company would suffer loss or damage if the directors were negligent in their actions or in the giving of advice.

11.5. Statute

S. 157(1) of the Act provides that a director shall, at all times, act honestly and use reasonable diligence in the discharge of the duties of his office. It would appear that the standard of diligence required in S. 157(1) of the Act is what is reasonable in the circumstances and no more, and this may vary according to the type of director.

As discussed earlier, the SC has stated in its Report that there is no need to exhaustively codify directors' duties, given that the Act already contains such a statutory statement on directors' duties. In addition, ACRA has also published a guidebook for directors. Hence, the SC and MOF have decided to keep the current status quo and will instead continue to monitor the developments in the UK and other jurisdictions.

Arising from this duty to be diligent, the following general propositions may be made:

(a) **A Director Is Not Required to Attend All Board Meetings**

Whether a director's failure to attend meetings amounts to a breach of his duty of diligence is a question of degree. Presumably, a high standard would have to be met by an executive director who had contracted to devote his full time and attention to the affairs of the company. Some articles also provide for the disqualification of directors should they be absent from meetings without permission for a specified number of times within a specified period.

(b) **A Director Is Not Liable for Loss Caused by Decisions Made at a Meeting That He Did Not Attend**

This is tied in to the fact that directors are not under a duty to attend all meetings. Accordingly, absent directors cannot be held liable for any loss caused by decisions or acts of the board taken or made in his absence on the grounds that had he so attended, he might have prevented the decision from being made or an act from being undertaken.

Furthermore, it would appear that a director is not under a duty to supervise the conduct of his codirectors.

However, a director may be liable for decisions made or acts undertaken in his absence if he had somehow authorised or consented to it.

11.6. Standard of Care and Skill

In determining whether there has been a breach by a director of his duty of care and skill, it is necessary to first establish the standard by which the acts and omissions of the director complained of can be measured against before a determination can be made as to whether there has been a failure to attain that standard.

The traditional approach to the standard of care expected of directors is that of "reasonable care". It would appear that a director need not exhibit a greater degree of care and skill than may reasonably be expected from a person of his knowledge and experience (<u>Lagunas Nitrate Co v Lagunas Syndicate (1899)</u>). Hence, the standard of test to be applied is subjective in nature, taking into account the director's personal characteristics and knowledge. The level of care and skill that is expected of a director will vary from individual to individual.

The modern approach, accepted in Singapore by CJ Yong in <u>Lim Weng Kee v DPP (2002)</u>, however, subjects the director to an objective standard. The director will be expected to exercise the same degree of care and diligence as a reasonable director found in his position. This standard will depend on various factors which include, *inter alia*, the director's role in the company, the type of decision being made and the size and business of the company. This standard will not be lowered to accommodate any inadequacies in the director's knowledge or experience. However, the standard will be raised if the director held himself out to possess some special knowledge or experience.

Closely connected with the exercise of reasonable care and skill is the question of diligence, in that a director who has exercised reasonable care and skill may still be in breach of his duty to be diligent. It may well be a play of words to say that evidence of lack of diligence may well help establish the failure to observe reasonable care and skill.

But regardless of how much care, skill and diligence is displayed by a director, it is impossible for him, either physically or professionally, to attend to all the affairs of the company personally. Accordingly, for all duties that may, having regard to the exigencies of the business and the articles of association, be delegated to some other official, a director is justified in trusting that official to perform such duties honestly unless there are reasonable grounds for suspicion, so that a director is not negligent merely because the person he trusted turned out to be a rogue. But if he knows of facts that should excite the suspicion of a reasonable man, he must make reasonable inquiries or face the consequences of his inaction. In considering what a director ought reasonably to have known or inferred, we need to take into account the knowledge, skill and experience which he actually had in addition to that which a person carrying out his functions should be expected to have. When it comes to the permissible delegation of duties of a director to some other person to be performed, there is a duty to exercise reasonable care to ensure that the person to whom the duties are delegated is competent to do so.

The court in <u>Vita Health Laboratories Pte Ltd v Pang Seng Meng (2004)</u> held that directors have a non-delegable duty of supervision that was objective. It approved the English decision of <u>Re Barings plc (No. 5) (2000)</u> which stated that directors have, both collectively and individually, a continuing duty to acquire and maintain a sufficient knowledge and understanding of the company's business to enable them properly to discharge their duties as directors. It further stated that whilst directors are entitled (subject to the articles of association of the company) to delegate functions to those below them in the management chain, and to trust their competence and integrity to a reasonable extent, the exercise of the power of delegation does not absolve a director from the duty to supervise the discharge of the delegated functions. The extent of this duty, and the question whether it has been discharged, must depend on the facts of each particular case, including the director's role in the management of the company. The holding of Vita Health in relation to the directors' non-delegable duty of supervision has been followed by the Singapore Court of Appeal in PlanAssure PAC (formerly known as Patrick Lee PAC) v Gaelic Inns Pte Ltd (2007).

However, nonexecutive directors may be held to a lower standard, given the fact that they do not participate in the management of the company on a full time basis. In Daniels v Anderson (1995), the court held that the nonexecutive directors of a company who negligently hired an employee who ran up massive liabilities were not liable on the basis that they were not involved in the day-to-day management of the company.

The area under the purview of directors that the courts will be most reluctant to review is one relating solely to business judgement. It is therefore said that honest directors are not liable for mere errors of judgement and the courts have acknowledged that the business decision of the directors will not be reviewed on its merits.

11.7. The Business Judgment Rule

Justice Tay in ECRC Land Pte Ltd v Ho Wong On Christopher (2004) stated that courts do not second-guess the commercial decisions of directors in acting in the best interests of the company. He added that a court should not, with the benefit of hindsight, substitute its own decisions in place of those made by directors in the honest and reasonable belief that they were in the best interests of the company, even if those decisions turned out subsequently to be money-losing ones.

In Ho Kang Pang v Scintronix Corp Ltd (2014), the Court of Appeal held that the best interests of a company is not limited to profit maximisation. It was also in the interests of the company to have their directors act within their powers and for proper purposes. Furthermore, continuing an improper practice by previous management without inquiring why it was made amounts to failure to exercise the duty of diligence and care that a reasonable director ought to have exercised.

Thus it can be seen that courts generally will not interfere with business decisions as long as the directors acted *bona fide*, and the decisions were independently made and informed. However, if there are allegations of fraud, breach of fiduciary duty and conspiracy, which occurred in ECRC Land, it is hard to imagine how the court will refuse to review the decisions of the directors involved.

Although decisions by directors are subjective in nature, they are usually subject to some form of an objective test. Justice Thean in Intraco Ltd v Multi-Pak Singapore Pte Ltd (1995) said that the test was whether an honest and intelligent man in the position of the directors, taking an objective view, could reasonably have concluded that the transactions were in the interests of the company. In applying this test, it is important to look at the matter without the benefit of hindsight. One must attempt to understand the transaction as it appeared at the time to the board. The holding of Intraco in relation to the non-interference by the courts of commercial decisions taken by directors have subsequently been followed in ECRC Land, Vita Health, and MacarthurCook Property Investment Pte Ltd and Another v Khai Wah Development Pte Ltd (2007).

The objective test was also illustrated in Australian Property Group Pte Ltd v H.A. & Chung Partnership and others (2015). The court held that appropriation of a company's funds for a director's personal use is a breach of director's duties to the company. The test is whether an honest and diligent man in their position could, in the circumstances, have reasonably believed that the use of such funds were for the company's benefit.

Unlike some Commonwealth countries, Singapore does not have a statutory business judgement rule. Such a rule would provide a presumption that a director had acted with due care and skill if certain pre-conditions are satisfied, in particular that the director acted honesty, rationally and was disinterested.

12. OTHER LIABILITIES OF DIRECTORS

12.1. Contracts by Directors Personally

There may be occasion where a director who is negotiating and entering into a contract on behalf of the company may be held to be a party to the contract instead of the company. It is a question of fact in each case whether the director was acting on behalf of the company or acting for himself.

In the case where contracts were made on behalf of a company that has not yet been incorporated, S. 41(2) provides that the person who purportedly acted on behalf of the company shall be personally bound by the contract unless there is an express agreement to the contrary or the contract has been subsequently ratified by the company after it has come into existence.

12.2. Breach of Warranty of Authority

Every agent acting on behalf of a principal and dealing with a third party impliedly warrants that he has sufficient authority from his principal in his dealings with the third party. Accordingly, if a director purportedly acts as agent for the company and it was subsequently found that the company does not exist or that the director did not have the requisite authority to bind the company to the transaction, then the third party may sue the director for breach of the implied warranty of authority.

12.3. Contracting of Debt Without Reasonable Expectation of Repayment (S. 339(3)) and Fraudulent and Wrongful Trading (S. 340)

If in the course of winding up, it is discovered that:

(a) an officer of the company was knowingly a party to the contracting of a debt and the officer had at that time no reasonable or probable ground or expectation that the company was able to pay the debt; or

(b) there was a person who was knowingly a party to carrying on of the business of the company with the intent to defraud the creditors of the company or creditors of any other person or for any fraudulent purpose,

then the liquidator, creditor or contributory of the company may apply to court for an order that the officer or person shall be personally responsible, without any limitation of liability, for the whole or any part of the debt in the first case or all or any of the debts or other liabilities of the company in the second case. A contravention of either also constitutes an offence punishable with a fine, imprisonment or both.

It is pertinent to note that pursuant to S. 340(2) of the Act, where an officer has authorised the contracting of a debt when he had no reasonable and probable expectation of the debt being repaid, the liquidator, creditor or contributory of the company may apply to make him liable to pay that debt only if he has been convicted of an offence under S. 339(3) of the Act. However, in the case of fraudulent trading under S. 340(1) of the Act, a conviction is not a prerequisite to an order that the officer assumes liability for the debts of the company.

While some English decisions such as R v Grantham (1984) have suggested an overlap between S. 339(3) and S. 340(1) of the Act on the basis that it might be legitimate to infer fraudulent intent where there was objectively no reasonable prospect of repaying a debt incurred, the bases of liability are clearly different. Proof of dishonesty in a personal, subjective sense is needed to establish fraudulent trading under S. 340(1) of the Act, although this will inherently involve consideration of the probability that the company would be able to trade out of its debts (Tang Yoke Kheng v Le Benedict (2005)). It is necessary to show that the creditor was deceived or misled in order to advantage the fraudster or cause loss to the creditor (Tang Yoke Kheng; Liquidator of Leong Seng Hin Piling Pte Ltd v Chan Ah Lek (2007)). In contrast, the basis of liability under S. 339(3) of the Act is focused on the expectation of repayment, and this is assessed objectively on the facts that were known to the defendant officer.

12.4. Payment of Dividends Other Than From Profits (S. 403)

Dividends can only be paid out of profits and every director who wilfully pays or permits dividends to be paid out of what he knows are not profits shall be guilty of an offence under S. 403(2)(a) of the Act and is also liable under S. 403(2)(b) of the Act to the creditors of the company for the amounts of the debts due by the company to them respectively, to the extent that the dividend paid out exceeded the profits.

The SC has considered the tests for dividend payments in jurisdictions like the UK, Australia and New Zealand and concluded that we should retain the current position, which is sufficiently well understood. It preferred to monitor the developments in other jurisdictions before reconsidering this issue. The MOF agreed with the SC's views in this regard.

12.5. Delinquent Officers (S. 341)

Under S. 341(1) of the Act, if, in the course of winding up, it is discovered that a person who has taken part in the formation or promotion of the company or any past or present officer of the company has misapplied, retained, become liable or accountable for any money or property of the company, or has been guilty of any misfeasance, breach of trust or duty in relation to the company, the court may on the application of the liquidator, creditor or contributory examine into the conduct of such person and compel him to repay or restore the money, property or any part thereof with interest at such rate as the court thinks just, or to contribute such sum to the assets of the company by way of compensation in respect of the misapplication, retainer, misfeasance or breach of trust or duty as the court thinks just.

S. 341(2) of the Act stipulates that S. 341 applies to the receipt of any money or property by any officer during the two years preceding the commencement of the winding up, whether by way of salary or otherwise, appearing to the court to be unfair or unjust to the other shareholders of the company.

13. EXONERATION OF DIRECTORS

13.1. Exemptions and Indemnities by the Company (S. 172)

Under S. 172(1) of the Act, any attempt, in any manner whatsoever, by the company to exempt or indemnify the directors from any legal liability that the directors may be subject to for any negligence, default, breach of duty or breach of trust that they may be guilty of in relation to the company shall be void.

There appears to be some uncertainty as to whether a company is prohibited under S. 172 from providing indemnity for claims brought by third parties. The term "in relation to the company" used in the prohibition in S. 172(1) has been interpreted in practice to also cover indemnity for claims brought by third parties since a director's liability in relation to the company may have repercussions on third parties.

However, as Singapore companies become more globalized, the risk of them being exposed to liabilities to third parties is real and should be addressed. The CA Amendments introduced a new S. 172B which allows a company to indemnify a director against third parties' liability. However, S. 172B provides that the indemnity cannot be provided for the following:

(a) payment of fines in criminal proceedings;

(b) payment of penalties in respect of regulatory non-compliance; and

(c) defending criminal proceedings where the officer is convicted and defending civil proceedings brought by the company or a related company in which judgment is given against the officer.

These changes will come into effect in Q1 2016.

A director may be released from his fiduciary duty and excused from liability for breaches of duty by members of a company acting together. Generally, if directors have exercised their powers irregularly without proper authority or acted for improper motives, they can obtain absolution. For the ratification to be effective, full and frank disclosure of all material facts, including the fact that there is a breach of duty, must be disclosed to members.

This power to release directors' liabilities is further subject to the condition that it must not amount to a fraud on the minority members or the creditors, oppression or disregard of a minority member's interests. The transaction must also not be illegal in the first place. The release will also be ineffective if it is procured by fraud or the concealment of relevant facts. Lastly, the members' power to release or ratify is effective only when the company is solvent.

13.2. Insurance

The prohibition in S. 172 applies to the company exempting or indemnifying the directors from their legal liabilities.

Accordingly, it would be open for directors to take up insurance policies to insure their own personal liabilities that may arise as directors, officers and employees of the company. The only legal concern is that under general insurance law, a person cannot insure against his own wilful or fraudulent act.

Naturally, the company itself can take up insurance policies to insure itself against any loss or damage suffered by it by reason of negligence of or breach of duty or trust by its directors and officers.

The position of whether the company can pay the premium on an insurance policy taken up by the director to insure his own personal liabilities was previously unclear. Under the CA Amendments, the new S. 172A will be similar to the current S. 172(2)(a) of the Act to the extent that a company can purchase an insurance policy for its directors to insure against any liability incurred by them except where the liability arises out of dishonest or wilful conduct.

13.3. Application to the Court for Relief (S. 391)

A director may apply to the court under this section for relief from a claim of negligence, default, breach of duty or breach of trust. The court may grant relief in respect of the whole or part of the liability provided that it is satisfied that he has acted honestly and reasonably and that, having regard to all the circumstances of the case including those connected with his appointment, he ought fairly to be excused from the negligence, default or breach. All three elements must be shown. It is only after it has been shown that the director had acted honestly and reasonably that the question of whether it is fair to excuse the director arises.

The court's power to relieve a director from liability only applies where the company is suing the director; it does not apply in actions brought by a third party against the director to enforce a civil liability.

In determining if a director had acted reasonably, the court will consider whether he has acted in the affairs of the company as he would have done in relation to his *own* affairs. The test appears to be semi-subjective and semi-objective: the court will consider the experience and qualifications of the person in question to determine if he had acted reasonably in the circumstances.

13.4. Release by the Company

At common law, a company may extinguish its right to sue a director by entering into a deed of release under seal or into a contract to release the director from liability in return for valuable consideration.

It seems arguable that if the company had promised or induced the director to believe that it would not sue him and he had acted in reliance on that promise, then the company may be estopped (prevented from denying the existence of a promise) from subsequently suing the director.

A board resolution to release the director (for example by approving the execution of the deed of release) would be ineffective as it would amount to a gift to a director, the gift being the company's right to sue, and directors have no power to make gifts to themselves.

Accordingly, such deed or contract of release must be approved by the majority of shareholders of the company after full disclosure of the facts. It is advisable that the director who is being released should abstain from voting if he also happens to be a shareholder, especially if he is the controlling voting power, as otherwise the release would appear to be invalid.

The ability of shareholders to release directors is subject to the following four limitations:

(a) the release must not amount to a fraud on the minority or the creditors or to oppression or disregard of a minority member's interests within the meaning of S. 216;

(b) the shareholders cannot ratify a transaction that is illegal;

(c) the 'release' will be ineffective if procured by fraud or by the concealment of relevant facts; and

(d) the shareholder's power to release is effective only when the company is solvent.

Some doubt has been expressed as to whether even the shareholders can forgive the breaches of a director without some kind of benefit to the company in return. Accordingly, in the case of Multinational Gas and Petrochemical Co v Multinational Gas and Petrochemical (Services) Ltd (1983), one judge was of the opinion that the company's right to sue for negligence must be considered as being part of the assets of the company and the shareholders of the company had a responsibility not to forego this right to sue unless it was reasonably incidental to the carrying on of the company's business and was made in good faith for the benefit of and to promote the prosperity of the company.

14. SHAREHOLDER REMEDIES

14.1. Oppression, Disregard of Member's Interests and Prejudice

S. 216(1) of the Act allows members of a company to bring an action against the company if there is oppression of a member, or where a member's interests are disregarded. It can also be used by members if a resolution or act of the company unfairly discriminates against or is otherwise prejudicial to a member.

S. 216(2) of the Act allows the court, if satisfied that the grounds have been established, to grant remedies which include an order cancelling the resolution or transaction, an order to regulate the conduct of the company's affairs in the future, an order authorising a derivative action, an order providing for the purchase of shares, an order providing for the reduction of a company's capital and a winding up order.

The SC considered whether to adopt a minority buy-out right or appraisal right as an alternative remedy for minority shareholders. The objective of such a right is to allow a minority shareholder, who dissented from certain fundamental changes to the enterprise or certain alterations of shareholder rights, to require the company to buy his shares at a fair value.

However, after considering the feedback from the public consultation, the SC decided that it was not in favour of introducing such a remedy. Although jurisdictions like New Zealand, the United States and Canada provide for a buy-out right or appraisal right, the SC noted that shareholders of Singapore incorporated companies generally have far more limited rights as compared to shareholders in the above-mentioned jurisdictions. In addition, the SC took the view that majority rule is part of the bargain that minority shareholders entered into, which includes the fact that their shareholder rights could be altered by special resolution. Hence, the the minority shareholders should not be able to require a buy-out on the ground that their rights had been altered or removed by special resolution. There is also concern that the introduction of such a remedy might lower the attractiveness of Singapore as a place for the setting up of businesses, and make it more difficult for entrepreneurs to change the course of their business. Instead, the SC recommended that S. 254(1)(i) and (f) of the Act should be amended to explicitly provide the court with the option, where the company is still viable, to order a buy-out instead of a winding-up where it is just and equitable to do so. The MOF agreed with the SC on this matter.

It should be noted that there is no inconsistency between S. 216 and the rule in Foss v Harbottle (1843) which prevents a member from suing to enforce a *company's* rights. A member suing under S. 216 is enforcing his *personal* right to be treated fairly (for example suing under a contract made with a member, or a tort committed against a member by the company).

To understand S. 216 of the Act, it may be useful to explain the meaning of the words ‘oppression’, ‘disregard’, ‘unfairly discriminate’ and ‘prejudice’.

(a) **Oppression**

The House of Lords defined ‘oppression’ in Scottish Co-operative Wholesale Society Ltd v Meyer (1959) as ‘burdensome, harsh and wrongful’. The Privy Council gave a broader definition to the word in Re Kong Thai Sawmill (Miri) Sdn Bhd (1978) by stating that the word ‘oppression’ refers to a visible departure from the standards of fair dealing and a violation of the conditions of fair play on which every member is entitled to rely.

(b) **Disregard**

The use of the word ‘disregard’ together with ‘oppression’ in S. 216 indicates that they do not have the same meaning, although there may be an overlap. The court in Re Kong Thai Sawmill (Miri) Sdn Bhd (1978) held that the word ‘disregard’ involved something more than a failure to take into account the minority’s interest. Rather, there had to be an awareness of that interest and an evident decision to override it or brush it aside or to set at naught the proper company procedure.

It should be noted that S. 216 does not grant a licence to a member of a company to bring an action against it merely because the management who possess a majority of the voting power uses the power to make policy or executive decisions which the member disagrees with. The judicial position is that shareholders have to accept the inevitable fact of majority rule in a company limited by shares.

S. 216 only comes into play when majority rule passes over into rule oppressive of the minority, or in disregard of the minority’s interests; there must be a course of conduct which in some identifiable respect, or at some identifiable point in time, which can be held to have crossed the line.

(c) **Discrimination**

‘Discrimination’ is said to exist within a company if one group of members is given a benefit which other members do not have, or where one group of members are subjected to some detriment or liability to which the others are not subject to.

It should be noted that because S. 216 uses the word ‘unfairly discriminates’, not all forms of discrimination are actionable under S.126. To illustrate this, the conferring of additional benefits to a class of members in a company, for example preference shareholders, will not be considered to be unfair discrimination because of their membership in the special class.

(d) **Prejudice**

‘Prejudice’ has been defined by English courts as ‘causing prejudice, detrimental to rights or interests’. Like ‘discrimination’, relief can only be granted for ‘prejudice’ if it is unfair and causes unjustifiable detriment to a member. If an act or resolution affects a member detrimentally but nevertheless is for the benefit of the company as a whole objectively, relief will not be available.

The House of Lords explained the basis of 'unfair prejudice' in the case of O'Neil v Phillips (1999). Firstly, the affairs of a company are conducted according to rules to which all shareholders have agreed to, usually with some formality such as the Articles of Association. Therefore, it is reasoned that relief will only be granted if there is a breach of the terms to which the member had agreed to.

Secondly, equity (the legal concept of fairness) will intervene in cases where equitable considerations make it unfair for those conducting the affairs of the company to rely on their strict legal powers. As such, unfairness may arise from a breach of the rules or in using rules in a manner which equity would regard as contrary to good faith.

14.2. The English Approach

The genesis of S. 216 is to be found in the UK Companies Act 1948. The UK Companies Act 1948 introduced a new provision, S. 210, to give a minority member an 'alternative remedy' to bringing a derivative action or petitioning to wind up the company on the just and equitable ground. S. 210 required oppressive conduct of the affairs of the company to be shown, and the House of Lords defined 'oppression' in Scottish Co-operative Wholesale Society Ltd as 'burdensome, harsh and wrongful'. Unfortunately, most cases of majority abuse of power consisted of conduct that was not independently unlawful or illegal, but rather an unfair exercise of majority power. Such conduct would not satisfy the oppression test in S. 210.

Subsequently, various amendments were made to S. 210 to broaden its scope, which became S. 75 of the Companies Act 1980 (now S. 994 of the UK Companies Act 2006). The 'oppression' test was thus substituted with 'unfair prejudice'.

14.3. The Australian Approach

The Australian approach appears to be broader than the English approach. Australian courts have held that the word 'oppressive' cannot be viewed in isolation. Rather, the words of the Australian equivalent of S. 216 have to be viewed as a composite whole. Therefore, one will have to ask whether, in the eyes of a commercial bystander, the conduct as a whole is so unfair that reasonable directors who consider the matter would not have thought the decision fair.

The High Court in Wayde v New South Wales Rugby League Ltd (1985) stated that the court will not intervene in cases of mere prejudice or discrimination. Intervention will only be possible if there is proof of oppression or unfairness.

14.4. The Singapore Approach

In Singapore, S. 216 of the Act appears to adopt four different tests: (i) oppression; (ii) disregard of interests; (iii) unfair discrimination; and (iv) prejudice. However, these four tests have been interpreted as alternative expressions of a single test broadly based on "commercial unfairness". The Singapore High Court held in Over & Over Ltd. v Bonvest Holdings Ltd (2008) that there is no meaningful distinction between all four limbs in S. 216 and that the common thread is some element of unfairness that would justify the invocation of the court's jurisdiction under S. 216. In Lim Swee Khiang v Borden Co (Pte) Ltd (2006), the Singapore Court of Appeal stated that the English provision 'corresponds materially' to S. 216, and approved of the leading English authority, O'Neill v Phillips (1999), which affirmed earlier English cases that commercial unfairness was the criterion of the English equivalent to Singapore's S. 216. Earlier, in Ng Sing King v PSA International Pte Ltd (No 2) (2005), the Singapore High Court also stated that it is now recognised that there should be no minute distinction between these individual terms in S. 216, and that the common thread underlying the entire section is the element of unfairness.

The concept of commercial unfairness provides the court with extremely wide discretion for determining when to intervene into corporate affairs to disrupt majority rule. This makes it extremely difficult to provide a general rule for what corporate conduct will offend the standard of fairness and lead to a successful action under S. 216. The starting point for determining commercial unfairness is the written agreement between the members (Re Saul D Harrison &

sons Plc (1995)). A member cannot normally claim unfairness unless there has been a breach of the articles (i.e., what is fair is what the members have agreed to). However, a minor breach of a rule, which does not produce unfairness, will clearly not support a remedy under S. 216. In fact, successful cases under S. 216, normally involve ongoing or multiple breaches that amount to commercial unfairness. However, where the majority's assertion of power complies with the written agreement between the members but conflicts with the legitimate expectations or equitable considerations of the minority members, the conduct of the majority can be challenged under S. 216. (Ng Sing King.) Legitimate expectations or equitable considerations arise out of informal *or* implied understandings *between* the shareholders which formed the basis of their association but were not put into contractual form.

The standard of fairness has not been specifically considered by the Singapore courts. However, persuasive English case law has adopted the position that commercial unfairness is to be determined on an objective standard (Re a company (No 005134 of 1986) ex parte Harries (1989); Re Saul D Harrison & sons Plc; O'Neill). This means that unfairness may be established even if the alleged wrongdoer did not intend to harm the complainant-member or did not believe the action to be wrong. However, what the objective standard is will depend on the context in which the dispute occurs (O'Neill). It remains to be seen if the Singapore courts will adopt a similar position.

Nonetheless, it is useful to examine the types of cases that tend to amount to commercial unfairness. However, it must be stressed that commercial unfairness is a malleable concept that must be proven in each individual case. The fact that a particular case appears to fit into one of the categories below may be a "red flag" for oppression—but is by no means determinative. Examples of commercial unfairness include the dominant members advancing their own interests (Lim Swee Khiang), abuse of voting powers (Re SQ Wong Holdings (Pte) Ltd (1987)), exclusion from management (Lim Swee Khiang; Ng Sing King), serious mismanagement (Lim Swee Khiang; Re Tri-Circle Investment Pte Ltd (1993)), no or inadequate dividends and/or excessive director compensation (Re Gee Hoe Chan Trading Co Pte (1991); Low Peng Boon v Low Janie (1999)) and loss of substratum (i.e., the fundamental basis upon which the parties enter into the corporate relationship) (Ng Sing King).

A S. 216 claim need not also be based on a corporate wrong. In Ng Kek Wee v Sim City Technology Ltd (2014), the Court of Appeal opined *obiter* that it was possible to succeed in a S. 216 claim even where there are no corporate wrongs at all. It further observed that in reality, there are often concurrent wrongs, comprising of a single wrongful act (normally a breach of directors' duties) which may amount to both a personal and corporate wrong.

14.5. Prerequisites for S. 216 to Operate

(a) Domination and Control

Relief under S. 216 can be obtained against persons holding the 'dominant power' in the company, and is not confined to majority shareholders. This is because majority shareholders, for a variety of reasons, may sometimes not be in control of the management of the company or the board.

However, the courts have also clarified that the mere fact that a shareholder is a majority shareholder does not preclude him from claiming relief under S. 216 (Sim City Technology). However, a majority shareholder would be precluded from claiming such relief if he possessed "the power to exercise self-help by taking control of the company and bringing to an end the prejudicial state of affairs".

(b) Mismanagement May Not Be Actionable

A member cannot seek relief under S. 216 merely because the majority exercises its voting power in favour of a policy or management resolution which the member disagrees with. The rationale for this is the Business Judgement Rule, which prevents the courts from inquiring into the rationality or prudence of a business decision unless there is fraud. However, the court in Ng Chee Kong v Ng Teong Kiat Highlands Plantation Ltd (1980) held that if the directors display complete indifference to the commercial interests of the company and let the business deteriorate to the point of inactivity, that might amount to oppressive conduct.

(c) **The Unfairness Must Affect the Petitioning Member in His Capacity as Member**

In order to get relief under S. 216, a member has to be affected by acts or decisions of the company as a *member*, and not in some other capacity such as a beneficiary under a family trust. In other words, the conduct complained of must have some connection with the affairs of the company.

(d) **Continuing State of Affairs**

In addition to the above, the oppression or disregard to a member's interest complained of have to be continuing at the time the action is brought. A member is not entitled to relief for oppression or disregard that has ceased. However, a petition under S. 216 may be based on a single act of which its consequences are several and continuing.

It has been suggested that in relation to an act or resolution that unfairly *discriminates* against a member, relief may be obtained even if the act or resolution has already been passed. The petitioner would probably have to show that the consequences of the act or resolution continue to affect him prejudicially or unfairly.

(e) **Relief to be Sought Expeditiously**

A petitioner should seek relief as soon as possible. Any delay may be construed by the court as a ratification of the acts or resolutions complained of.

(f) **Burden of Proof**

The petitioner has to prove to the court on a balance of probabilities the acts complained of. The more serious the allegations, the higher the standard of proof necessary to make good such allegations. Likewise, the more serious the relief sought (such as a winding-up order), the heavier the burden would be on the petitioner to establish a case for relief.

14.6. Suits on Behalf of the Company (S. 216A)

(a) **Background**

In accordance with the 'proper plaintiff' rule (derived from the rule in Foss v Harbottle (1843)), an injury to the company should be brought by the company itself, since it is a separate entity in the eyes of the law. One of the rationales for the rule is, *inter alia*, the avoidance of multiple suits by individual shareholders on the same subject.

However, because a company has no physical existence, a person or body of persons have to act as 'the company' for the purpose of authorising litigation. If the articles of association do not specify the person or persons responsible for authorising litigation, the managing director usually has the implied authority to commence or defend proceedings in the name of a company (Avel Consultants Sdn Bhd v Mohd Zain Yusof (1984)).

The issue of the person or persons responsible for litigation choosing not to sue may sometimes arise. For example, the person may want to avoid negative publicity for the company, preserve a business relationship with an important customer, or the person responsible for suing may be the wrongdoer himself.

A member choosing to sue defendants in his own name would have to do so under a derivative action. It is 'derivative' because the member is not suing to enforce his own rights, but the company's. Any right that he has 'derives' from that of the company. Hence, any remedies will go to the company and not himself since he is enforcing the company's rights.

(b) **Operation of S. 216A**

S. 216A was enacted in 1993 to clarify the uncertainty surrounding the common law derivative action. S. 216A introduced a two-part procedure. Firstly, a complainant, usually a member, has to apply to court for leave to commence an action on behalf of a company. Secondly, if leave is granted, the complainant has to take the necessary steps to initiate the action using the company's name.

While members would normally make such applications, the court has the discretion to allow other persons to apply. An individual director can apply under S. 216A for leave to bring proceedings in the company's name (Agus Irawan v Toh Teck Chye (2002)).

S. 216A goes further than the common law derivative action in that it allows a complainant to intervene in or defend an *existing* action. This gives the complainant a chance to intervene if the directors are not conducting the litigation properly. It should be noted that S. 216A does not abolish the common law derivative action, but rather, S. 216A acts as an alternative to the common law derivative action. However, listed companies do not have this alternative available to them and have to rely on the common law derivative action (S. 216A(1)).

The CA Amendments expanded the ambit of S. 216A. A complainant may now apply to the court for leave to commence arbitration in the name and on behalf of the company. He may also intervene in an arbitration to which the company is a party for the purpose of prosecuting, defending or discontinuing the arbitration on behalf of the company. These changes came into effect on 1 July 2015.

Further, the statutory derivative action is now available to Singapore-incorporated companies that are listed for quotation or quoted on a securities market, whether in Singapore or overseas.

For an action under S. 216A, it is pertinent to note that the loss suffered must be to the company and not the shareholder. As with a common law derivative action (or any action), a statutory derivative action cannot be brought when the company's claim that is being advanced is based on a shareholder's reflective loss, unless one of the exceptions to the reflective loss principles applies (Townsing Henry George v Jenton Overseas Investment Pte Ltd (in liq) (2007); Hengwell Development Pte Ltd v Thing Chiang Chin (2002)). A reflective loss involves either a decrease in the value of the shareholder's shares in the company or the amount received by the shareholder as dividends from the company.

However, two exceptions to the no-reflective loss rule exist (Hengwell Development Pte Ltd v Thing Chiang Chin (2002)):

(i) Where the company has no cause of action to recover its loss

This may occur where the company may not be able to pursue its claim because of the actions of the wrongdoer or because the company is in a jurisdiction that has no proper remedy.

In Hengwell Development Pte Ltd v Thing Chiang Chin (2002), the plaintiff, Hengwell ("**H**"), was the majority shareholder of a Singaporean unlisted joint venture company ("**JVC**"). Far East Packaging Industrial Pte Ltd ("**FE**") was Hengwell's minority partner in the JVC. The only business of the JVC was that of a wholly owned China subsidiary ("**Q**"). Under the JV agreement FE was granted day-to-day control of Q. H claimed that the directors appointed by FE to Q misappropriated funds from Q by making fraudulent misrepresentations (with the assistance of FE) to Q and the JVC. Thus, H claimed that FE and the directors appointed by FE breached their contractual and fiduciary duties owed to Q and the JVC. However, an action could not be commenced against the directors of Q by Q's board because the board was controlled by the wrongdoer directors and there was no derivative action (or any equivalent) under Chinese law. The JVC also could not commence an action against Q's directors and FE because there was no quorum at the JVC's directors meeting. Therefore, H sought leave to commence a S. 216A derivative action in the name of the JVC for damages flowing from the misappropriated funds. In response, the defendants claimed that the JVC had no standing as it had merely suffered a reflective loss (i.e., the loss in the value of its Q shares). The court held that as there was no risk of double recovery, the policy reasons for the no reflective loss rule did not apply. In addition, Q has no cause of action or is unable to enforce its full rights under Chinese law. Therefore, H was allowed to bring a S. 216A in the name of the JVC for recovery of the damages resulting from the misappropriated funds

(ii) Where the shareholder suffers a loss separate and distinct from that suffered by the company

This may occur where the shareholder has a right to sue another shareholder for a breach of their shareholders' agreement, which is separate from the right of the company to sue the defaulting shareholder.

In the English case of Giles v Rhind (2002), G and R had been members in a company which became insolvent following the diversion by R of a contract to a third party, in contravention of a shareholders' agreement. The company discontinued its proceedings against R as a consequence of its insolvency, but G sought to pursue in his own right damages against R. G contended that his claims were not merely reflective of the company's loss. Accepting this argument, the English Court of Appeal held G had a cause of action against R separate from that of the company. In any case, with regard to G's losses which reflected those of the company, G was entitled to proceed with his personal claim, as the company had been prevented from pursuing its own action as a result of R's wrongdoing.

(c) **Procedure**

Complainants seeking relief under S. 216A of the Act must first give notice to the directors 14 days before an application for leave is brought before the courts, in accordance with S. 216A(3)(a) of the Act. This is to give them an opportunity to commence the action themselves. The notice should specify what the complainant wants the directors to do, the causes of action and any other material particulars. Thereafter, if the directors do not respond with a good reason, or make a decision not to commence proceedings that was not honestly arrived at, the complainants should commence the suit by originating summons. The court may grant leave to the complainant after considering the facts of the case.

To be granted leave, S. 216A(3)(b) and (c) provide that the complainant has to satisfy the court that he is acting in good faith, and it appears *prima facie* in the interests of the company that the action should be brought. Like common law derivative actions, the court in a S. 216A proceeding presumably has the discretion to refuse leave if the complainant does not come to court with 'clean hands', i.e., he is guilty of some wrongdoing himself, or where there is unreasonable delay in bringing the action (Nurcombe v Nurcombe (1985)).

(i) **Good Faith**

In order to get relief under S. 216A, a complainant has to commence proceedings in good faith. The institution of proceedings because of personal considerations, or a vendetta to damage or destroy the company will indicate a lack of good faith (Pang Yong Hock v PKS Contracts Services Pte Ltd (2004)).

The court in Re Bellman and Western Approaches Ltd (1981) held that commencing an action under S. 216A concurrently with a personal action under S. 216 does not necessarily indicate bad faith.

The *onus* is on the *defendant* to establish that the complainant is not acting in good faith. The defendant must demonstrate something more than hostility between the parties to establish that the plaintiff is not acting in good faith (Pang Yong Hock). When the action is clearly within the best interests of the company to pursue, the defendant will likely have to show that the action is frivolous, vexatious or devoid of absolutely any merit to establish bad faith (Richardson Greenshields of Canada v Kalmacoff (1995)).

It should also be noted that good faith needed under S. 216A(3)(b) is good faith with respect to commencing the derivative action, not good faith generally in all the past conduct of the applicant (Pathak v Mooloo (2008)).

(ii) ***Prima Facie* in the Interest of the Company**

The complainant also has to show that the relief sought is *prima facie* in the interest of the company. Two elements have to be proved to establish this.

Firstly, there must be a reasonable basis for the complaint and a legitimate or arguable case against the proposed defendants (Re Winpac Paper Products Pte Ltd (2000); Teo Gek Luang v Ng Ai Tiong (1999)). The complainant need not prove facts in dispute, but has to show that the company will stand to gain substantially in money or money's worth (Agus Irawan v Toh Teck Chye (2002)). It is not necessary for him to show that there is a likelihood of success. The judge has the discretion for refusing leave if it appears that the action is vexatious or frivolous (Teo Gek Luang). Generally, the courts take a cautious approach rather than a liberal approach in deciding whether to grant leave, in order to prevent disgruntled members from 'driving the corporate vehicle from the backseat'.

Secondly, the complainant has to show that it is in the interests of the company that the case be pursued. The broad commercial interests of the company must be considered (not just the monetary amount of the claim) when determining if it is in the company's interests. If pursuing the action will not make sense commercially, leave will not be granted. Whether there are other adequate remedies may also be considered in refusing to grant leave (Pang Yong Hock v PKS Contracts Services Pte Ltd (2004)). However, merely because there is an alternative remedy is not alone a sufficient reason for the court to refuse leave (Ting Sing Ning v Ting Chek Swee (2008)).

If the complainant manages to satisfy the court of the above, the onus will shift to the directors to explain why it would not be in the interests of the company to do so. The fact that the majority shareholders have decided not to pursue the action will be taken into account but will not be a decisive factor (S. 216B).

The same principles apply *mutatis mutandis* where leave is sought to intervene in or defend an existing action (Kiyue Co Ltd v Aquagen International Pte Ltd (2003); Ng Heng Liat v Kiyue Co Ltd (2003).)

(d) **Costs**

In contrast to common law derivative actions which usually require a complainant to bear the costs of the action, S. 216A(5)(c) of the Act allows the court to make an order requiring the company to pay reasonable legal fees and disbursements incurred by the complainant. If the court deems fit, it may order a partial indemnity (Turner v Mailhot (1985)). However, it should be noted that since the dispute is between the minority shareholders and the directors, the directors have no right to use company funds to pay for their costs on the application for leave (ex p Johnson (1992)) and to finance their defence if leave is given to sue.

(e) **Withdrawal**

A complainant cannot, without approval of the court, discontinue or settle an action under S. 216A once leave has been granted (S. 216B(2)).

15. THE SINGAPORE CODE ON TAKE-OVERS AND MERGERS

15.1 Overview

The Take-Over Code is issued by MAS under S. 321 of the SFA. While it does not have force of law, failure to comply may be relied upon by a party to a criminal or civil proceeding to establish or negate any liability in question in the proceeding (S. 321(5) of the SFA).

The Take-Over Code applies to both take-overs and mergers. The Take-Over Code also applies to all schemes of arrangement, trust schemes and amalgamations with exemptions from certain provisions of the Take-Over Code. Entities subject to the Take-Over Code include corporations and business trusts with a primary listing of their securities and units respectively in Singapore. The Take-Over Code also applies to real estate investment trusts ("**REITs**"). Private companies are exempt from the Take-Over Code.

The following types of entities may also be required to observe the letter and spirit of the General Principles and Rules under the Take-Over Code, where possible:

(a) unlisted public companies with more than 50 shareholders and net tangible assets of $5 million or more; and

(b) unlisted registered business trusts with more than 50 unitholders and net tangible assets of $5 million or more.

A fundamental objective of the Take-Over Code is to ensure that only shareholders have the right to determine the merits of an offer. As such, the Take-Over Code contains Rules and General Principles that clarify a director's duties under a take-over.

15.2 General Principles

The Take-Over Code comprises of 13 General Principles. These principles are meant to supplement areas which are not explicitly covered by any Rule. The General Principles also seek to regulate the acts of directors and protect shareholders.

General Principle 4 provides that rights of control must be exercised in good faith and oppression of the minority is wholly unacceptable. General Principle 8 also imposes an obligation on the offeree board to seek independent advice in the interests of its shareholders. Under Rule 7.1 of the Take-Over Code, the board of an offeree company must obtain competent independent advice on any offer and the substance of such advice must be made known to its shareholders.

Directors are also under a fiduciary duty to act in the best interests of shareholders in a take-over. General Principle 13 requires directors to have regard to the interests of shareholders as a whole. Directors should also refrain from acting on their own interest or those derived from personal or family relationships.

Finally, General Principle 11 establishes the standard of care for documents issued to shareholders in connection with an offer. It states that any document containing recommendations from directors of an offeror or offeree should, as with a prospectus, meet the highest standards of care and accuracy.

15.3 Frustration of Offers by an Offeree Board

Rule 5 of the Take-Over Code provides that the offeree board must not take any action without shareholders' approval that may result in any *bona fide* offer being frustrated.

Examples include the sale of disposal of assets of material amounts, and entering into contracts otherwise than in the ordinary course of business.

The rationale for Rule 5 is to prevent offeree directors from independently affecting the state of affairs of the offeree company to provide grounds for withdrawal of the offer.

This Rule is a reiteration of General Principle 7 of the Take-Over Code which restricts what directors may do when faced with a *bona fide* offer. The purpose is to provide shareholders with an opportunity to decide an offer on its merits.

However, Rule 5 has led to some uncertainty as to what would amount to frustrating a *bona fide* offer. In particular, the SIC acknowledged the possibility of offeree boards misconstruing Rule 5 as prohibiting the soliciting of a competing offer.

Consequently, the Take-Over Code Amendments seek to clarify the application of Rule 5. Accordingly, an offeree board that solicits a competing offer would not be deemed to frustrate an offer as the original offer will still be available for shareholders' consideration.

The proposed amendments to Rule 5 were prompted by concerns raised by the public and media in relation to the take-over of Fraser & Neave ("**F&N**") in 2012. During the competitive bid for F&N, questions were raised as to whether F&N was able to seek a better offer. The SIC clarified that the Take-Over Code does not prohibit the offeree board from soliciting competing offers.

15.4 Directors' Responsibilities

The Take-Over Code also codifies a board's responsibilities in a take-over situation. Rule 6 states that directors must ensure that proper arrangements are in place to enable them to fulfil their responsibilities under the Take-Over Code.

In general, these arrangements should comprise of the following:

(a) ensuring that directors are provided with all relevant documents, announcements and information in connection with the offer;

(b) ensuring that directors with a day-to-day responsibility for the offer are able to justify to the board their actions and proposed causes of action; and

(c) ensuring that the opinions of advisers are available to the board where appropriate.

Rule 8.3 of the Take-Over Code also requires directors of the company issuing a document or advertisement in connection with an offer to assume responsibility for its contents.

Delegation of responsibility to a committee of the board for supervision of documents is also permitted under the Take-Over Code. However, each of the remaining directors of the company must reasonably believe that the persons to whom supervision has been delegated are competent (Note 2 on Rule 8.3).

In addition, each director must also disclose the following to the committee:

(a) all relevant facts directly relating to himself (including close relatives, related trusts and companies controlled by him etc); and

(b) all other relevant facts and opinions held by him which, to the best of his knowledge and belief, are either not known to any member of the committee or are unlikely to be considered by the committee during the preparation of the document.

15.5 Conflicts of Interest

Directors who may face conflicts of interests are also required to consult the SIC on whether it is appropriate for them to assume responsibility for any recommendations the board may make on the offer to its shareholders.

A director of an offeree company who agrees to become a director, employee or nominee of the offeror is normally exempt from responsibility for any recommendations on the offer (Note 1 on Rule 8.3).

15.6 Break Fees

A break fee arrangement is allowed where an agreed fee is paid by the offeree to the offeror if a specified event occurs that prevents the success of the offer. The Take-Over Code imposes certain safeguards with regards to break fees.

In particular, the directors of the offeree company and its financial adviser are required to provide the following confirmations to the SIC where a break fee is proposed:

(a) that the break fee arrangements were agreed as a result of normal commercial negotiations;

(b) that all other agreements in relation to the break fee arrangements have been fully disclosed; and

(c) that each of the directors and financial adviser believe the fee to be in the best interest of the offeree's shareholders.

As mentioned, the business judgment of directors will not be second-guessed if exercised in good faith. In a take-over, this means that the recommendation of independent directors to an offer is seldom questioned.

In the context of break fees, confirmation that the fee is "in the best interest of the offeree's shareholders" is also an application of the business judgment rule. Accordingly, the SIC is unlikely to second guess the business judgment of an offeree's directors when such confirmation is given.

16. CONCLUSION

In conclusion, it is not merely an honour to be elected to a board of directors. As explained in the discussion above, directors are subject to many onerous duties and responsibilities both at common law and by legislation. This is due to the need to protect shareholders and those who deal with the company from the negligence or misfeasance of errant directors, who are often in control of the management of a company. As seen in the preceding section, members of a company are able to bring actions against malfeasant or errant directors. Thus, the position of director should only be considered by those with a wealth of experience in business and management, who are therefore able to run a company competently.

GLOSSARY OF TERMS

Unless otherwise defined, certain key terms used in this article shall bear the following meanings:

"Act"	:	means the Companies Act, Chapter 50 of Singapore;
"ACRA"	:	means the Accounting and Corporate Regulatory Authority of Singapore;
"AGM"	:	means the annual general meeting of a company;
"Audit Committee"	:	means the audit committee of a company;
"CA Amendments"	:	means the Companies (Amendment) Act 2014;
"CEO"	:	means the chief executive officer of a company;
"Chairman"	:	means the chairman of the board of directors of a company;
"General Principles"	:	means the general principles as set out in the Take-Over Code;
"Governance Code"	:	means the Code of Corporate Governance 2012;
"IPO"	:	means initial public offering;
"Listing Manual"	:	means the Listing Manual of the SGX;
"MAS"	:	means the Monetary Authority of Singapore;
"MOF"	:	means the Ministry of Finance of Singapore;
"Nominating Committee"	:	means the nominating committee of a company;
"Q1 2016"	:	means the first quarter of 2016;
"Remuneration Committee"	:	means the remuneration committee of a company;
"SC"	:	means the Steering Committee appointed by the MOF to revamp the Act;
"SFA"	:	means the Securities and Futures Act, Chapter 289 of Singapore;
"SGX"	:	means the Singapore Exchange Securities Trading Limited;
"SIC"	:	means the Securities Industry Council;
"Take-Over Code"	:	means the Singapore Code on Take-Overs and Mergers;
"Take-Over Code Amendments"	:	means the proposed amendments to the Take-Over Code; and
"Table A"	:	means the sample set of articles of a company provided in the Fourth Schedule of the Act.