Directors' statutory duties under the Companies Act

Section 157 of the Act sets out the statutory duties of directors. Firstly, directors in discharging their duties, have a statutory duty at all times to (a) act honestly and (b) use reasonable diligence. Secondly, officers and agents of the company cannot make improper use of any information acquired by virtue of their position to gain, directly or indirectly, (a) an advantage for himself or for any person, or (b) to cause detriment to the company. This is often referred to as a fiduciary duty. A director is an officer of the company. The extensive application of this statutory fiduciary duty to anyone who is deemed to be an officer or agent of the company has significant implications for the corporate governance responsibilities of those persons.

The statutory duties of a director, officer or agent under section 157 are in addition to, and not in derogation of, any other written law or rule of law relating to the duty or liability of directors or officers of a company. A director's breach of this statutory duty can be a civil breach rendering the director liable to the company for any profit made by him or for any damage suffered by the company. The breach can also be a criminal offence.

DIRECTORS' FIDUCIARY DUTIES UNDER THE COMMON LAW

A director is regarded as a fiduciary both at common law and under the Act. A fiduciary relationship arises when one party (the company) is entitled to expect that the other party (the director) will act in the first party's interests to the exclusion of the second party's separate interests. Of all the duties of a director, his fiduciary duty is conceptually the most demanding. It is an all encompassing duty. A director's duty is not merely to serve the company's interests. He must avoid placing himself in a position where he prefers his own interests, or the interests of a third party, instead of or to the detriment of the company's interests. This fiduciary duty is also a statutory duty under section 157(2) of the Act. As the application of the fiduciary duty is very broad, this duty may be recognised under the following rules under the common law :

1. a director has to act bona fide in the interests of the company and not for any collateral purpose. In doing so, the director must make sure he does not in any way benefit from the act of good faith or have any interest whatsoever in the act. Unlike a trustee, a director can exercise his own interest so long as he has obtained the company's fully informed consent. This consent must be obtained through a full disclosure of all the facts and of the director's own interests in the transaction.

2. where a director is required to act bona fide in the interest of the company, he must act according to what he thinks, not what a court may consider, is in the interest of the company. This duty is therefore subjective. Commonwealth and Singapore cases have affirmed that the court will not consider a director to have breached his duty merely because it is the court's opinion that the particular act was not in the company's interest. However this does not mean that the court takes a back seat. The court must consider on points of law whether the directors had really acted bona tide and in the interest of the company.

3. the Singapore Court of Appeal held that the correct test in determining whether the directors have acted bona tide 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. Merely acting bona fide in itself is not sufficient.

4. a director has to act for the proper purposes of the company. 'Proper purpose' refers to a purpose which is for the benefit of the company. What is a 'proper purpose' is not always discernible. Where the purposes of the company are not defined in the articles of association, the matter has to be resolved by the court based on the facts of the case including an examination of the articles of association of the company.

5. where a particular power is exercised for more than one purpose, the "but for" test is useful in ascertaining whether an act is exercised in the best interest of the company. Would the director have exercised the particular power or act if not for the improper purpose? If the answer is yes, the substantive test of proper purpose is satisfied and the director is regarded as having exercised his power in the best interest of the company. In the Singapore case of Banque Bruxelles Lambert & Ors v Puvaria Packing Industries (Pte) Ltd (in liq), the Court of Appeal held that the mere fact that some benefit accrued to the respondent company did not mean that the transaction was for the purposes of the company.

6. There is a clear difference between acting in the best interest of the company (a subjective test) and acting for the proper purposes of the company (an objective test). Sometimes the two duties conflict. A director may be guilty of not acting for the proper purposes of the company even though there is no bad faith, he was not motivated by self-interest and he genuinely believed that what he did was in the best interest of the company.

7. a director is under a strict liability not to place himself in a position of conflict of interest vis—a—vis the company. He must avoid placing himself in a position where his own interest could potentially conflict with that of the company's interest. The test is 2 would a reasonable man looking at the relevant facts and circumstances of the case think that there was a "real and sensible possibility of conflict?" The attitude of the Singapore courts is clearly seen in Lim Koei Ing v Pan Asia Shipyard & Engineering Co Pte Ltd ..

8. a director in a position of potential conflict of interest can ameliorate his liability by (a) full disclosure at the first instance to the board or to the shareholders in general meeting; (b) abstaining from any discussions or voting on the matter; and (c) absenting himself from the board meetings. This duty is also found in s.l56 of the Act. In one of the few Singapore cases where a person was successfully prosecuted for a criminal breach of s.l56, the High Court held that the Act imposed a duty of disclosure on a director who held a directorship in another company so long as there was a potential conflict of duty. S.156(5) did not require the director to have a personal interest that in fact give rise to a conflict.

9. a director is strictly prohibited from making any profit or gain following his breach of duty. A director is liable to account to the company for any profit he makes from his breach, notwithstanding that the company itself could not have made that profit or suffers no loss. This was affirmed by the Singapore High Court in Hytech Builders Pte Ltd v Tan Eng Leong & Anor.

10. the rule of "no secret profit" is applied so strictly that even if there is no realistic possibility of conflict between the interest of the company and the duty of the director, so long as the director has made a profit which is sufficiently connected with his fiduciary office, an account of the profit is required. In the landmark English case of Regal (Hastings) Ltd v Gulliver, the House of Lords held that the directors of the plaintiff had to account for the profit made as the profit arose in the execution of their fiduciary duties as directors. There was no dispute that the directors were honest and well-intentioned, there was no bad faith. The House of Lords rejected the Court of Appeal's argument that once the directors came to a bona fide decision that the company could not take up the opportunity, the directors' obligation to refrain from taking up the opportunity for themselves ceased. Their Lordships recognised that the person in a fiduciary position might be the only person in the world who could not avail himself of the opportunity. This was not true absolutely since all that a director needs to do was to obtain the consent of the shareholders to secure his freedom to make the profit for himself. Failing that, the only course open to the director was to let the opportunity pass.

THE SINGAPORE CORPORATE GOVERNANCE ENVIRONMENT

In Singapore, shareholders have the right to ensure that a company is properly run. This right is enforced via the derivative action. In fact any person whose interests have been, are or would be affected by the conduct or likely conduct of another person in contravention of the Singapore Companies Act (“the Act”) can apply for an injunction. Similarly that same aggrieved person may apply for an injunction to require a person to do an act or thing that he is required to do by the Act.

Directors are also required to have regard to the interests of the company’s employees generally (as well as the interests of its members) in exercising their powers. Singapore’s corporate governance regime does not require that employees be represented on the board or on committees of the board, as is the practice in, for instance, Germany. The powers of a company shall, if these powers would not otherwise do so, be deemed to include the power to provide for employees on cessation of business. The applications of these sections of the Act have not been tested in the Singapore courts.

Creditors are not specifically protected under the Act except in so far as the security rights of secured creditors are recognised in situations where a receiver, a judicial manager or a liquidator is appointed. Creditors have some measure of protection in that it is a criminal offence for any officer of the company to knowingly contract a debt when there is no reasonable or probable ground to expect that the company can pay the debt. Any creditor may apply to the Court for a declaration that any person who knowingly carries on the business of the company with intent to defraud creditors shall be personally responsible for all of the debts and liabilities of the company. An important deterrent for directors is section 406 of the Act which makes it a criminal offence to induce creditors to give credit to the company by deceitful, fraudulent or dishonest means; and to defraud creditors by effectively removing the property of the company beyond the reach of creditors.

ARE DIRECTORS' DUTIES OWED TO THE COMPANY OR TO THE SHAREHOLDERS?

Directors must exercise the powers vested in them collectively as a board and not individually. The directors are duty-bound to remain impartial as between groups of shareholders in the company. The SGX Listing Manual recognises this principle when its rules require that an independent financial adviser be retained to advise minority shareholders on a material interested person transaction. The directors' duty is owed to the body of shareholders as a whole. However, in the governing and management of the company, the classic view, decided in 1902 in Percival v Wright, is that fiduciary duties of the directors are owed to the company only.

This View is increasingly challenged in cases in Australia, New Zealand and England starting with Coleman v Myers, Peskin v Anderson, Glandon Pty Ltd v Strata Consolidated Pty Ltd, and the more recent well—known case of Glavanics v Brunninghausen. The Court of Appeal in Brunninghausen v Glavanics held that although a director's fiduciary duties are owed to the company and not to the shareholders, where a particular transaction does not concern the company but only another shareholder, this should not preclude the recognition of a fiduciary duty to the shareholders in circumstances where this duty would not compete with the fiduciary duty to the company. This paper will not go further into this developing area of the law.

To summarise, factors that may give rise to a director's fiduciary duty to shareholders include : (a) the existence of a relationship of confidence as in Coleman v Myers, this is likely to apply to Singapore companies where a liability may arise through a family relationship; (b) limited number of shareholders; (c) dependence on the directors for full and relevant information; (d) where directors mislead the shareholders; and (e) positive action on the part of directors to persuade or induce the shareholders to a course of action. In the Singapore case of T at Kim San & Anor v Lim Cher Kia, the High Court considered the line of cases enumerated above, and held that on the facts, the director did not owe a fiduciary duty to the particular shareholders in a transaction where the managing director purchased the shares of two shareholders.

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Information is not advice. If in doubt you should consult your professional adviser.