LEGAL UPDATE

Recent Developments in Singapore Relating to Directors' Duties

19 September 2018

For any queries relating to this article, please contact:

Christopher Tan
christophertan@leenlee.com.sg

Authors:
Christopher Tan
Cherlyn Lee

Lee & Lee
50 Raffles Place, #06-00 Singapore Land Tower, Singapore 048623
T : +65 6220 0666

Introduction

1. Recently, there have been a number of Singapore court decisions which discuss the content of the duties owed by directors. This update seeks to highlight some of the more significant cases.

2. In *Sakae Holdings Ltd v Gryphon Real Estate Investment Corp Pte Ltd and others (Foo Peow Yong Douglas, third party) and another suit* [2017] SGHC 73 ("***Sakae Holdings***"), the High Court found that a person who had resigned as a director from a company but continued making key strategic and investment decisions for the company, was a shadow director. As such, he could be liable for breach of fiduciary duties.

3. In *Ho Yew Kong v Sakae Holdings Ltd and other appeals and other matters* [2018] SGCA 33 ("***Ho Yew Kong***"), the Court of Appeal held that a director's duties of care, skill and diligence are different, and distinguishable from his fiduciary duties.

4. In *Goh Chan Peng and others v Beyonics Technology Ltd* [2017] SGCA 40 ("***Beyonics Technology***"), the Court of Appeal confirmed that the test for whether a director has acted honestly and bona fide in the best interests of the company has both subjective and objective elements.

5. In *Parakou Investment Holdings Pte Ltd and another v Parakou Shipping Pte Ltd (in liquidation) and other appeals* [2018] SGCA 3 ("***Parakou***"), the Court of Appeal decided that when a company is insolvent, directors can still be held liable for breach of fiduciary duties even though the transactions they made on behalf of the company could not be clawed back in a claim for undue preferences under the Companies Act.

6. In *Traxiar Drilling Partners II Pte Ltd (in liquidation) v Dvergsten, Dag Oivind* [2018] SGHC 14 ("***Traxiar Drilling***"), the High Court emphasised that when a director directs a group of companies, he must not act with the intention of furthering the interests of the group as a whole to the prejudice or detriment of a company within the group.

***Sakae Holdings* – Shadow director liable for breach of fiduciary duties**

7. The High Court in *Sakae Holdings* held that a person who did not have the title of director but made major corporate decisions for the company was a shadow director, and could be liable for breach of fiduciary duties.

Facts

8. Sakae Holdings Ltd ("**Sakae**") entered into a Joint Venture Agreement ("**JVA**") with Griffin Real Estate Investment Holdings Pte Ltd ("**GREIH**") in September 2010. The purpose of the joint venture was to enable GREIH to invest in the building in Victoria Street known as "Bugis Cube" with a view to selling the investment for a profit.

9. Sakae claimed that after signing the joint venture in 2010, it and Douglas Foo ("**Foo**", the Chairman of the Board of Sakae) had subsequently left the management of the company to Andy Ong. In the following years, Sakae alleged that Andy Ong, Ho Yew Kong ("**Ho**") and Ong Han Boon had allegedly diverted the assets of the Company to the ERC Group over the course of seven transactions, allegedly without Sakae's knowledge.

10. In October 2012, Foo started to have serious concerns about some of the transactions. He convened a Sakae board meeting in October 2012 to inform the board about his concerns. Thereafter, Sakae conducted investigations into GREIH's financial affairs, and found questionable transactions. The discoveries caused Sakae to institute court proceedings.

Claims before the High Court

11. Sakae brought a suit against the following Defendants, including:

    a. Griffin Real Estate Investment Company ("**GREIC**"), the first defendant

    b. ERC Holdings Pte Ltd ("**ERC Holdings**"), the second defendant

    c. Andy Ong, Ho and Ong Han Boon, the third, fourth and fifth defendants, allegedly directors of the company at all material times.

12. Sakae claimed against the Defendants for relief for minority oppression under the Companies Act. It also claimed against Andy Ong, Ho and Ong Han Boon, for wrongfully diverting moneys from the GREIH over the course of seven transactions.

13. In relation to Sakae's claims against Andy Ong, Ho and Ong Han Boon, the High Court judge had to determine whether these defendants were directors of the Company at all material times, and hence whether they were subject to the duties that had allegedly been breached.

14. Andy Ong and Ong Han Boon were both formally appointed directors of the Company on March 2008 and October 2010 respectively. They resigned in early 2012, and were ostensibly replaced by Ho. Furthermore, in March 2015, Ho resigned. Andy Ong and Ong Han Boon were reappointed as directors.

15. The High Court judge found that Andy Ong was a shadow director of GREIH from March 2012 until up to Ho's resignation, but not Ong Han Boon. As such, Andy Ong was subject to the usual duties (including fiduciary duties) incumbent on a director for the period from March 2012 until up to Ho's resignation.

16. Consequently, Ong Han Boon and Ho were subject to fiduciary duties only during the periods they held the formal appointment as directors. For Ong Han Boon, this was from October 2010 to March 2012; for Ho, this was from February 2012 to March 2015.

17. The High Court judge noted that there are different types of directors: those who are formally appointed ("**de jure**") and a puppeteer pulling the strings from above (a "**shadow director**"). Whether he is a de jure director or shadow director, under the Companies Act and at general law, such a person owes the same duties to the company as a formally appointed director.

18. In particular, a shadow director is a person in accordance with whose directions or instructions the directors of a corporation are accustomed to act, even though he claims not to be a director. Whether someone is a shadow director is a question of fact and degree.

19. On the facts, the High Court judge found that Andy Ong was a shadow director even from October 2012 onwards, even though he had ostensibly resigned as director. This was because Andy Ong was the one who agreed to allow Sakae access to GREIH's documents and to decide whether Sakae could obtain documents relating to GREIH's financial affairs.

20. Furthermore, Ho (ostensibly the replacement director for Andy Ong and Ong Han Boon) was given very little information about GREIH when Andy Ong approached him to be a director. Ho did not ask for further information about GREIH even after he accepted the appointment. The Judge found that Andy Ong acted unilaterally in key areas of corporate decision-making, and Ho relied on Andy Ong's instructions to the point of unquestioning deference.

21. Since Andy Ong was a shadow director, he owed fiduciary duties to Sakae from October 2012, which he had breached on the facts.

22. However, the High Court judge was not convinced that Ong Han Boon was a shadow director after March 2012, because there was little evidence that he had control of GREIH's affairs after that period.

***Ho Yew Kong* – Directors' duties of care, skill and diligence distinct from their fiduciary duties**

23. The Court of Appeal in *Ho Yew Kong* held that a director's duties of care, skill and diligence are distinguishable from his fiduciary duties.

Facts

24. The relevant facts are the same as in the previous case mentioned, *Sakae Holdings.* The dispute stems from the ill-fated joint venture agreement between Sakae and GREIH.

25. In this case, Sakae brought a claim against inter alia, Ho Yew Kong ("**Ho**"), Andy Ong and the ERC Group alleging that they had acted in a manner oppressive to its interests as a minority shareholder

in GREIH. In particularly, Sakae sought to argue that Ho had breached his fiduciary duties as a director of GREIH, and had thus oppressed Sakae.

Is there a distinction between breach of duties of care, skill and diligence, versus breach of fiduciary duties?

26. Although a company director is a fiduciary, not all the duties which he owes his company are fiduciary duties (duties founded in a director's duty of loyalty to his company). A director's duties of care, skill and diligence are not fiduciaries duties because they are not imposed to exact loyalty from a director.

27. On the facts of *Ho Yew Kong*, Ho signed the Lease Agreement on Andy Ong's instructions without making any enquiries to satisfy himself that it was in the Company's interest. The Court of Appeal held that it was negligent of Ho to make such enquiries and in doing so he had breached his duties of care, skill and diligence. However, that did not make him dishonest in and of itself, and did not show that he had acted in breach of his fiduciary duties to GREIH.

When will a director's breach of his duties of care, skill and diligence amount to minority oppression?

28. A director's breach of his duties of care, skill and diligence in monitoring the management of his company's affairs would amount to minority oppression under s216 of the Companies Act only if the negligent mismanagement was sufficiently serious.

29. However, on the facts, the Court of Appeal held that Ho's negligence was not sufficiently serious to amount to commercial unfairness, and thus did not constitute minority oppression.

Beyonics Technology **– Test for whether a director acted bona fide in the best interests of a company**

30. In *Beyonics Technology*, the Court of Appeal decided that the test for whether a director acted bona fide in the best interests of a company has both subjective and objective elements, but courts in practice often apply a more objective test.

Facts

31. Goh Chan Peng ("**Goh**") was a director of several companies in the Beyonics group of companies ("**Beyonics Group**"). In this business, there were two relevant competitors, Nedec Co Ltd and Kodec Co Ltd (collectively, "**NedKo Group**").

32. One of its divisions, Beyonics Technology Ltd ("**BTL**") supplied baseplates to a key customer, Seagate Technology International ("**Seagate**"). Due to a disruption in its supply of baseplates in October 2011, Seagate was anxious to secure capacity.

33. Hence, Seagate proposed an alliance between Beyonics Group and NedKo Group to supply baseplates to it. However, Goh was instrumental in causing Seagate to approve the alliance. He did so by under-representing BTL's capacity to produce baseplates. This led Seagate to believe that Beyonics Group needed to collaborate with NedKo Group in order to meet Seagate's demand for

baseplates. However, the High Court judge found that BTL actually had sufficient production capacity to handle Seagate's demand by itself.

34. Consequently, in November 2011, Seagate approved of the alliance between Beyonics Group and NedKo Group.

35. Furthermore, Goh was the one who initiated the idea of asking for a US$2.5m grant from Seagate for NedKo Group, and used his presentation slides in a meeting between BTL, Seagate and NedKo Group to push for the grant.

36. In addition, Goh had set up a corporate entity in the British Virgin Islands called Wyser-I, which he was the beneficial owner of.

37. In April 2012, Goh signed two agreements on behalf of Wyser-I. The first agreement was between Wyser-I and Kodec, the second was between Wyser-I and Nedec. Both agreements were backdated to November 2011 (when Seagate had approved of the collaboration between Beyonics Group and NedKo Group), and provided for payments to be made to Wyser-I. Goh received some of the money paid under the Agreements. Collectively, they are known as the "**Wyser payments**". BTL claimed that the payments were bribes, but Goh claimed the payments were for consultancy services rendered.

38. BTL sued Goh, inter alia, for breaching his contractual, statutory and fiduciary duties to Beyonics Group, in that:

    a. He secured the alliance between Beyonics Group and NedKo Group, thereby effecting a diversion of business of producing baseplates away from Beyonics Group.

    b. He procured the Seagate grant for NedKo Group which assisted it in boosting its technical capabilities and helped it grow as a supplier of baseplates to Seagate.

    c. He received payments for assisting in securing the Seagate grant to NedKo Group (the Wyser payments).

What is the test for whether a director acted bona fide in the best interests of a company?

39. The test for whether a director acted bona fide in the best interests of a company has both subjective and objective elements. The subjective element lies in the court's consideration as to whether a director had exercised his discretion bona fide in what he considered (and not what the court considers) is in the interests of the company. Thus, a court will be slow to interfere with commercial decisions made honestly but which, on hindsight, were financially detrimental to the company.

40. The objective element in the test is that the court has to assess whether an intelligent and honest man in the position of a director of the company concerned could, in the whole of the existing circumstances, have reasonably believed that the transactions were for the benefit of the company.

41. The Court of Appeal endorsed the observation (in *Walter Woon on Company Law*) that the courts in practice often apply a more objective test.

42. On the facts, the Court of Appeal upheld the High Court's findings that Goh breached his duty to act in the best interests of the company. It found that Goh's actions were not in BTL's best interests from an objective point of view, thus an inference could be drawn that he was not acting honestly. BTL could have handled the business itself without the alliance as it had sufficient production capacity, and the first appellant's actions to assist the NedKo Group were not in BTL's best interest.

43. Furthermore, where a director is found to have placed himself in a position of conflict of interest, he will not be permitted to assert that his action was bona fide or thought to be in the interests of the company. On the facts, Goh's actions were tainted by the receipt of payments for his assistance to NedKo Group, thus he could not assert that his actions were bona fide.

When do payments made to directors violate the no-profit and no-conflict rules?

44. The no-profit rule obliges a director not to retain any profit made through the use of the company's property, information or opportunities to which he has access by virtue of being a director, unless he has the fully informed consent of the company. The no-profit rule is a particular application of the no-conflict rule, i.e. that a fiduciary may not obtain profit in connection with his position without the informed consent of the person he is duty-bound to protect.

45. Goh argued that, inter alia:

    a. The payments under the Wyser Agreements did not breach the no-profit rule as they were not made to him qua director of BTL;

    b. Goh had informed the chairman of BTL that he may be entering into consultancy agreements with NedKo Group; and

    c. The Wyser Agreements did not breach the no-conflict rule as his consultancy services were in the best interests of BTL.

46. The Court of Appeal rejected all his arguments.

47. His first argument was a misrepresentation of the law: payments that flout the no-profit rule need not strictly flow to the fiduciary qua director. Instead, the profit merely has to be obtained in connection with his position as a director. On the facts, this was met: Goh was able to make a secret profit because he was CEO of Beyonics Group.

48. His second argument was erroneous – the information which Goh had disclosed was lacking in detail. In particular, he had not disclosed that payment for the services would be made to him personally. Even if the disclosure was full, Goh would not be released from his obligations to the company since he had only made his disclosure to the chairman. However, the chairman did not constitute the entirety of the board of directors.

49. Even if the work done under the Wyser Agreements was in the best interests of BTL, all the more the no-conflict and no-profits rules would still be engaged. This is because if a director accepts payment in consideration for acting in a certain way in relation to the company's affairs, he would clearly be in breach of his fiduciary duty.

50. Hence, the Court of Appeal upheld the High Court's finding that the payments made under the Wyser Agreements were to be characterised as bribes.

***Parakou*- Directors' fiduciary duties owed to creditors of an insolvent company outside the statutory clawback period**

51. In *Parakou*, the Court of Appeal re-emphasised the duties which directors owe to the company's creditors when a company is insolvent or approaching insolvency. The Court decided that directors can be liable for breach of fiduciary duties even though the relevant transactions that they caused the insolvent company to enter into fell outside the statutory clawback period. Where the transaction is outside the statutory clawback period, the party seeking recovery must prove that the acts are in breach of fiduciary duties. In seeking to prove a breach, the mere fact of payments to related parties is not sufficient.

Facts

52. Parakou was a company with a ship chartering business. In 2008, the Directors of Parakou (the "**Directors**") purportedly caused Parakou to enter into a charterparty with regard to a vessel (the "**Canton Trader**") which Parakou was to charter from Galsworthy Limited ("**Galsworthy**"). Parakou planned to sub-charter the vessel to another company. However, following a collapse in the freight market in September/October 2008, the other company no longer wished to sub-charter the vessel.

i. The London Arbitration and Hong Kong Court Proceedings (The "Legal Proceedings")

53. As such, in February 2009, Parakou informed Galsworthy that it would not execute the charterparty, claiming that it was not valid. Galsworthy then commenced arbitration proceedings against Parakou in London (the "**London Arbitration**"). Parakou then commenced court proceedings in Hong Kong against the owners of the "Canton Trader" for an indemnity in respect of any liabilities it might incur in the London Arbitration (the "**Hong Kong Court Proceedings**"). Collectively, they are known as the "**Legal Proceedings**".

ii. The Disputed Transactions

54. Furthermore, within a period of less than two months, from November to December 2008, Parakou carried out a series of rapid disposals of its assets, including:

a. repaying debts of more than S$9 million that it had owed to Parakou Investment Holdings Pte Ltd ("**PIH Repayments**");

b. providing bonus payments to the Directors ("**Bonus Payments**");

c. increasing the monthly salaries of 2 of the Directors ("**Salary Increases**").

55. Collectively, Parakou's rapid disposals of its assets in the series of transactions listed above are known as the "**Disputed Transactions**".

Claims before the High Court

56. The Liquidators claimed that the Directors had breached their fiduciary duties by, inter alia, entering into the Disputed Transactions and by continuing the London Arbitration proceedings as well as commencing the Hong Kong court proceedings.

57. The High Court judge held that the Directors had carried out most of the Disputed Transactions in breach of fiduciary duty. However, he held that the Directors had not breached their duties by continuing the London Arbitration proceedings and commencing the Hong Kong court proceedings.

58. Before the Court of Appeal, in their respective appeals, the Liquidator and Defendants appealed most of the findings which the High Court judge had made against them.

Did the Directors breach their fiduciary duties?

i. London Arbitration and Hong Kong Court Proceedings

59. The Court of Appeal held that the Directors' decision to commence and/or continue the London Arbitration and Hong Kong Court Proceedings was in breach of their fiduciary duties.

60. First, the Court of Appeal found that a key concern of the Directors in commencing and/or continuing these proceedings was avoiding the statutory clawback period, but such avoidance was not in the creditors' best interests. The two-year clawback period for undue preference claims expired in December 2010, but Parakou was wound up in 2011. Thus, the Liquidator would have been able to lay claim to the Disputed Transactions as undue preferences but for the fact that they took place outside the clawback period.

61. With regard to the Hong Kong court proceedings, the Hong Kong counsel for Parakou noted his understanding that Parakou might be able to "hold off winding up proceedings in Singapore on the basis of a pending appeal in Hong Kong". Emails between the Hong Kong counsel and the Directors made it plain that their focus was on delaying Hong Kong court proceedings sufficiently until the clawback period had expired. Since the High Court judge and parties were content to treat the Hong Kong court proceedings and London Arbitration as two integral parts of the same strategy executed by the Directors, both legal proceedings were commenced and/or continued in breach of the Directors' fiduciary duties.

62. In addition, the amount of legal costs incurred suggested that the proceedings were not in the creditors' best interests. The Directors had only offered Galsworthy a settlement proposal of US$3,000,000, indicating that that was the maximum they thought the claim was worth. However, they had incurred around $6m in legal costs, twice the amount of the settlement proposal. This was unlikely to be in the creditors' best interests because, even if the settlement were reached, the effective amount taken to have reached the settlement would be three times what the Directors themselves valued the claim at.

ii. The Disputed Transactions

63. The Court of Appeal held that in respect of the PIH Repayments, Bonus Payments and Salary Increases, the Directors had breached their fiduciary duties.

64. An issue common to three payments made by the Directors (the PIH Repayments, Bonus Payments, and Salary Increases) was that Parakou was in a bad financial state at that time. Since the Galsworthy Claim had to be taken into account in assessing Parakou's liabilities, Parakou was in reality insolvent at the material time (i.e. November 2005). As such, since Parakou was not making a profit and the Directors had no reason to believe that this was the case, then there could have been no genuine commercial reason to make the Bonus Payments and Salary Increases. The Directors also ought not to have made the PIH Repayment if they knew or ought reasonably to have known that Parakou would not benefit from those repayments being made at the material time.

65. The High Court judge had held that a claim for breach of fiduciary duty by the Directors in respect of the PIH Repayments may be brought despite the two-year clawback period for undue preferences having expired. The Court of Appeal approved that decision: because the two claims are premised on separate causes of action, therefore they should be maintainable both independently and concurrently. Nonetheless, where the transaction is outside the statutory clawback period, the party seeking recovery must prove that the acts are in breach of fiduciary duties. In seeking to prove a breach, the mere fact of payments to related parties is not sufficient.

What remedies are there against directors who breach fiduciary duties?

66. The Court of Appeal held that the innocent party can elect between damages and an account of profits. An account of profits is available against a fiduciary who procures an unlawful benefit for a corporate vehicle in which he had a substantial interest, particularly where the corporate vehicle was a mere cloak for his unlawful conduct.

67. On the facts, the Liquidator was entitled to elect between damages and an account of profits as between the relevant wrongdoers jointly and severally.

Traxiar Drilling- director of a group of companies must act in good faith towards the interests of each individual company

68. The High Court in *Traxiar Drilling* held that a director of a group of companies must act in good faith towards the interests of each individual company. Nonetheless, failing to act bona fide in a company's interests is not the same as committing fraud.

Facts

69. The Plaintiff company, Traxiar Drilling Partners II Pte Ltd ("**Traxiar**") was incorporated in Singapore by the defendant, Dag Oivind Dvergsten ("**Dvergsten**"), and Dvergsten was a director of Traxiar.

70. Traxiar attempted to acquire a jack-up drilling rig (the "**Somnath**"), and in connection with its purchase, Dvergsten negotiated for Traxiar to enter into various loan transactions. Traxiar was eventually unable to acquire the Somnath and was wound up by an order of court.

Claims before the High Court

71. The Liquidators brought a case against Dvergsten, alleging that inter alia:

a. Dvergsten had breached his duties to act honestly in the discharge of his duties as a director under s 157(1) of the Companies Act and/or his duty to act bona fide in the interests of the Plaintiff under the common law in carrying out the loan transactions;

b. Dvergsten had breached his duty to take into account the interests of Traxiar's creditors, dissipating his assets to the creditors' prejudices by making unjustified payments to his own companies;

c. Dvergsten had intended to defraud Traxiar's creditors in contravention of s 340(1) of the Companies Act.

72. The High Court judge held that Dvergsten had breached his directors' duties; however, he could not conclude that Dvergsten had committed fraud.

How does a director's duty to act in good faith apply when he directs a group of companies?

73. A director's duty of honesty and duty to act in good faith is a composite obligation, which imposes a unitary obligation to act in good faith in the interests of the company in the performance of one's functions as director.

74. When the director directs a group of companies, the director must still act in good faith toward the interests of each individual company. Thus, a director must not act with the intention of furthering the interests of the group as a whole to the prejudice or detriment of a company within the group. This flows from the fact that a company is a separate legal entity, and the fact that the liabilities of the company do not ordinarily attach to its shareholders or officers.

75. On the facts, Dvergsten had breached his duty to act bona fide in the interests of Traxiar.

Under what circumstances will a director be considered to have acted fraudulently?

76. For fraudulent trading under s 340(1) of the Companies Act to be made out, the party making the claim had to show that: 1) the company's business had been carried out with the intention of defrauding the company's creditors or creditors of any other person or for any fraudulent purpose and 2) the Defendant was knowingly a party to the business being carried out in that manner. However, on the facts, the 1st element had not been made out.

77. For fraud to be shown, there were likewise 2 elements which needed to be shown: 1) an element of dishonesty which results in the deception of a creditor, and 2) that the director had intended to gain an advantage.

78. On the facts, while the High Court judge found that Dvergsten had not acted bona fide in Traxiar's interests, he could not conclude that Dvergsten had committed fraud. None of Dvergsten's actions (even him keeping the loan money in his own company's account rather than using it to secure the purchase of the Somnath, or his misrepresentation to a loan company about the use of the first tranche of funds), were sufficient to convince the High Court judge that Dvergsten intended to defraud the loan company. There was an alternative explanation that could justify these actions.

LEGAL UPDATE

About Lee & Lee

Lee & Lee is one of Singapore's leading law firms being continuously rated over the years amongst the top law firms in Singapore. Lee & Lee remains committed to serving its clients' best interests, and continuing its tradition of excellence and integrity. The firm provides a comprehensive range of legal services to serve the differing needs of corporates, financial institutions and individuals. For more information: visit www.leenlee.com.sg.

The following partners lead our departments:

Kwa Kim Li
Managing Partner
kwakimli@leenlee.com.sg

Quek Mong Hua
Litigation & Dispute Resolution
quekmonghua@leenlee.com.sg

Owyong Thian Soo
Real Estate
owyongthiansoo@leenlee.com.sg

Tan Tee Jim, S.C.
Intellectual Property
tanteejim@leenlee.com.sg

Adrian Chan
Corporate
adrianchan@leenlee.com.sg

Louise Tan
Banking
louisetan@leenlee.com.sg