# CHAPTER 1

# DIRECTORS

## I. INTRODUCTION

1 The Steering Committee for Review of the Companies Act has reviewed the key provisions in the Companies Act relating to directors and directors' duties, with a view to identifying areas which would benefit from reform and refinement. This chapter sets out the Steering Committee's recommendations arising from the review. In particular, it relates to the meaning of shadow director, appointment of directors, qualifications of directors, disqualification of directors on conviction of certain offences, vacation of office and removal of directors, payment of compensation to directors for loss of office, loans to directors and connected companies, the supervisory role of directors, power of directors to bind the company, power of directors to issue shares of company, directors' fiduciary duties, imposition of liability on other officers, disclosure of company information by nominee directors and indemnity for directors.

## II. SHADOW DIRECTORS

2 "Director" is defined in section 4(1) and (2) of the Companies Act to include "a person in accordance with whose directions or instructions the directors of a corporation are accustomed to act". Such a person is commonly referred to as a shadow director. The term "shadow director" is not used in the Act.

3 The Steering Committee does not see any necessity to have a separate definition for shadow director. This view was supported by the majority of the respondents during the focus group consultation. However, the Steering Committee considered whether it would be useful for the Companies Act to clarify that a person who controls all the directors or the majority of the directors is a shadow director.

4 The English court in *Ultraframe (UK) Ltd v Fielding and others; Northstar Systems Ltd v Fielding and others*[1] held that a person at whose direction a governing majority of the board was accustomed to act was capable of being a shadow director. The court took the view that there was difficulty as a matter of language in construing the phrase "the directors of the company" in section 741 of the UK Companies Act 1985[2] as meaning "some of the directors of the company" or even "a majority of the directors of the company". However, the policy underlying the definition was stated to be that a person who effectively controlled the activities of a company was to be subject to the same statutory liabilities and disabilities as a person who was a de jure director.

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[1] [2005] EWHC 1638 (Ch); [2005] All ER (D) 397.

[2] Section 741(2) of the UK Companies Act 1985 provided that in relation to a company, "shadow director" means a person in accordance with whose directions or instructions the directors of the company are accustomed to act.

5 This must be read subject to the views of the Court of Appeal of Singapore in *Heap Huat Rubber Company Sdn Bhd v Kong Choot Sian*[3], where it was held that it was a matter of construction of the articles of association whether a "shadow director" had to comply with formal requirements. Since the extended definition of "director" in section 4(1) only applies where the context allows, it would similarly be a matter of construction whether any particular section or regulation applies to shadow directors.

6 A refinement to the meaning of shadow director to refer to control of the majority of the directors would be consistent with the definition of "shadow director" in Hong Kong. Section 2 of the Hong Kong Companies Ordinance defines a "shadow director" in relation to a company as "a person in accordance with whose directions or instructions the directors or a majority of the directors of the company are accustomed to act". The Hong Kong definition by making a reference to the words "a majority of the directors" makes it clear that a person is a shadow director if he controls all the directors or a majority of the directors, but he is not a shadow director if he controls only one director or a minority of the directors. The Steering Committee is of the view that the Hong Kong definition provides greater clarity.

7 The definition of "director" in the Australia Corporations Act 2001 which includes shadow director and the definition of "shadow director" in the UK Companies Act 2006 do not contain any express reference to "the majority of the directors".

8 The Steering Committee considered whether to adopt the English and Australian approach of not having any express reference to "the majority of the directors". One view is that it is not necessary to have such express reference as we could rely on the common law position. However, there is another view that there would be greater clarity if it is expressly provided in the Companies Act that a shadow director includes a person who controls the majority of the directors. In the interests of certainty and clarity, the Steering Committee recommends the latter.

9 During the focus group consultation, the majority of the respondents were in favour of amending the definition of "director" in section 4(1) and (2) of the Companies Act to clarify that a person who controls the majority of the directors is also to be considered to be a director. It was felt that this would be an appropriate definition for shadow director (without necessarily using the term in the Act), and such an amendment would be useful clarification.

10 There were, however, some concerns that the proposed amendment would not be sufficiently robust to address situations where a person is able to exert significant influence over the company even though he does not control the majority of the directors. For example, in the case of a delicately balanced or split board, a person who controls an independent director may be able to exert significant influence on board matters and decisions. There were also concerns that the proposed amendment would not be adequate to address the situation where a person controls one dominant member of the board, who in turns influences the rest of the board. That person should also be regarded as a shadow director.

11 The Steering Committee considered all the feedback received and is of the opinion that a person who controls a single director on the board should not be deemed to be a shadow director. The issue goes beyond influence and control as shadow directors are subject to the obligations and duties of directors as set out in the Companies Act and at common law.

[3] [2004] SGCA 12.

It would be too harsh to subject a person who controls only one director to all the obligations and duties of a director.

12 Further, this would result in corporate shareholders which nominated directors to the boards of companies being regarded as shadow directors. This may in turn result in corporate shareholders owing duties of care to one another in closely held joint venture companies. The Steering Committee considered whether it would be desirable to expressly exclude such corporate shareholders from the meaning of shadow director, but felt that it was not necessary to have such exclusion. The issue whether a corporate shareholder could be regarded as a shadow director in a situation where its nominee director did not exercise independent judgment and only acted in accordance with the instructions of his corporate shareholder should be left to the court if such a case arises.

**Recommendation 1.1**

**It is not necessary to have a separate definition of "shadow director" in the Companies Act.**

**Recommendation 1.2**

**The Companies Act should clarify that a person who controls the majority of the directors is to be considered a director.**

## III. APPOINTMENT OF DIRECTORS

### *(a) Mode of appointment*

13 The Companies Act does not prescribe how directors are appointed; this is left to the companies' articles of association. Typically, directors are elected by the members at the annual general meeting of the company.[4]

14 Table A which contains default articles makes provision for the appointment of directors[5]. 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 Table A is excluded by the company's articles.

15 Having an express provision in the Companies Act will simplify matters as a company will not have to provide for the appointment of directors in its articles or rely on Table A, unless the company wishes to provide for a different mode of appointment. The

[4] *Walter Woon on Company Law*, 3rd Ed, 2005, at paragraph 2.27.

[5] Article 67 provides that the company may from time to time by ordinary resolution passed at a general meeting increase or reduce the number of directors. Article 68 provides that the directors shall have power at any time, and from time to time, to appoint any person to be a director, either to fill a casual vacancy or as an addition to the existing directors, but so that the total number of directors shall not at any time exceed the number fixed in accordance with Table A. Articles 91 and 94 provide for the appointment of managing directors and associate directors respectively.

Steering Committee received industry feedback that in practice, Table A is often excluded by the companies' articles as it is not found to be useful.[6]

16 The current Singapore approach of not prescribing in legislation how directors are appointed is consistent with the position in the UK and Hong Kong. The Steering Committee considered whether the Companies Act should expressly provide for the mode of appointing directors, following the position in Australia and New Zealand.

17 For reasons of simplicity and greater clarity, the Steering Committee recommends that the Companies Act should provide expressly that unless the articles provide otherwise, a company may appoint a director by ordinary resolution passed at a general meeting. The mode of appointment is subject to the company's articles to give flexibility to companies.

18 This approach is consistent with that in Australia where the statutory provisions in the Australia Corporations Act 2001[7] on the mode of appointing directors are replaceable rules.[8] It is also consistent with the approach in the New Zealand Companies Act 1993 where section 153(2) provides for the appointment of subsequent directors by ordinary resolution, unless the constitution of the company otherwise provides.

19 During the focus group consultation, the majority of the respondents expressed support for having such an express provision on the appointment of directors in the Companies Act. It was felt that notwithstanding that there is little dispute in practice on how directors are appointed, it would be good to clearly provide that the general meeting has power to appoint directors, subject to contrary provision in the articles.

**Recommendation 1.3**

**The Companies Act should provide expressly that a company may appoint a director by ordinary resolution passed at a general meeting, subject to contrary provision in the articles.**

***(b) Approval for assignment of office***

20 Section 170 of the Companies Act provides that if in the case of a public company, provision is made by the articles or by agreement between any person and the company empowering a director or manager to assign his office to another person, the assignment is of no effect until approved by a special resolution of the company.

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[6] It should be noted that the Steering Committee has recommended that the current Table A be replaced by a Model Constitution: see Chapter 5, recommendations 5.7 and 5.8.

[7] Section 201G of the Australia Corporations Act 2001 provides that a company may appoint a director by resolution passed in general meeting. Section 201H(1) provides that the directors of a company may appoint a person as a director and a person can be appointed as a director in order to make up a quorum for a directors' meeting even if the total number of directors of the company is not enough to make up that quorum.

[8] Both sections 201G and 201H of the Australia Corporations Act 2001 are replaceable rules, that is, provisions that can be displaced or modified by the company's constitution (section 135(2)).

21 The Steering Committee recommends that section 170 should be repealed as it is now obsolete. Today, there is no assignment of office as new directors are appointed. In any case, office is personal in nature and should not be transferable or assignable.

22 During the focus group consultation, the majority of the respondents were in favour of repealing section 170 as it no longer fulfils any useful function and is rarely used in practice. It was also noted that the English equivalent provision[9] had been repealed.

**Recommendation 1.4**

**Section 170 of the Companies Act requiring approval for assignment of office of director or manager should be repealed.**

## IV. QUALIFICATIONS OF DIRECTORS

### *(a) Corporate directorships*

23 Under section 145(2) of the Companies Act, only a natural person who has attained the age of 18 years and who is otherwise of full legal capacity can be a director of a company. The requirement for a natural person has been in the Companies Act since 1967.

24 The Steering Committee considered a proposal to allow corporate directorship in Singapore. It was argued that the availability of corporate directorship in Singapore would encourage the growth of company incorporations in Singapore, especially from foreigners who would otherwise take their business elsewhere where corporate directorship is available[10].

25 Corporate directorship is not allowed in Australia, Canada, New Zealand, Malaysia and the US (under its Model Business Corporations Act). In the UK, corporate directorship is allowed but only in a restricted form, that is, at least one director must be a natural person[11]. The Hong Kong Government has proposed a restriction of its corporate directorship regime, which currently permits corporate directorship in private companies with shares not listed in a recognised stock market, by requiring every private company to have at least one director who is a natural person.[12]

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[9] Section 308 of the UK Companies Act 1985.

[10] Corporate directorship is available in some offshore jurisdictions such as the Cayman Islands and the British Virgin Islands.

[11] The UK Companies Act 2006 requires every company to have at least one director who is a natural person so that someone may, if necessary, be held accountable for the company's actions. The UK Government had in its company law review considered the abolition of corporate directorship but was concerned that an outright ban of corporate directors might harm those companies which made use of the flexibilities in corporate directorship for entirely legitimate reasons. For example, a parent company may like to be a corporate director of its subsidiaries to facilitate group cohesion.

[12] Hong Kong Government's Consultation Conclusions on Company Names, Directors' Duties, Corporate Directorship and Registration of Charges dated 10 December 2008, available at http://www.cr.gov.hk/en/publications/consultation.htm.

26 The Steering Committee has found no compelling reason to allow corporate directorship in Singapore, especially in view of the difficulties in determining the person who is actually controlling the company and accountability of corporate directors. Furthermore, a number of major jurisdictions have moved away or are moving away from corporate directorship.

27 Based on the feedback received during the focus group consultation, there was almost a consensus that there is no need for corporate directorships in Singapore.

**Recommendation 1.5**

**It would not be necessary to allow corporate directorships in Singapore.**

***(b) Training of directors***

28 The Companies Act currently does not prescribe the academic or professional qualifications of directors. The Companies Act also does not provide for the training of directors.

29 The Steering Committee does not see any compelling reason for the Companies Act to prescribe the academic and professional qualifications of directors. The current position in Singapore is consistent with that in the UK, Australia, New Zealand and Hong Kong.

30 The Steering Committee is also of the view that the Companies Act should not mandate the training of directors.[13] A mandatory requirement would not necessarily ensure that directors are of good quality and may instead have the effect of deterring potentially good candidates from accepting directorship. The training of directors in Singapore is presently undertaken through non-legislative means, which is working well. For example, the Singapore Institute of Directors conducts extensive and systematic training for directors.

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On 2 April 2008, the Hong Kong Government launched a public consultation on whether to abolish corporate directorship altogether or restrict it in the same manner as that in the UK Companies Act 2006, so as to improve the accountability and transparency of company operations and the enforceability of directors' obligations.
It was noted that one feature of corporate directorship was that the delegate might change from time to time, making it very difficult to know who was responsible for the conduct of the business of a company. Further, as the delegate of a corporate director was not personally a director of that company, his duties were not owed to the company and it would be difficult to attach to him liability for acts or omissions prejudicial to the company. Therefore, in the interest of improving corporate governance which stressed a high degree of disclosure and transparency, corporate directorship should be abolished, subject to a grace period. On the other hand, there were concerns that abolition of corporate directorship would drive away many private companies established in Hong Kong and would have adverse implications for businesses, in particular, the ability to incorporate companies quickly and the flexibility provided by corporate directorship in the management of companies set up purely for asset holding purposes. Further, there were legitimate reasons for corporate directorship, for example, a parent company may like to be a corporate director of its subsidiaries to facilitate group cohesion.
In view of the equally strong opinions received during the public consultation exercise on the need to enhance corporate governance and transparency and the legitimate commercial need for flexibility, the Hong Kong Government found that the UK approach of requiring at least one director to be a natural person would strike an appropriate balance between the two.

[13] However, in the case of the listed companies, training of their directors may be provided in the Code of Corporate Governance or the Listing Manual, if the Singapore Exchange Limited (SGX) decides that it would be desirable to do so.

31 During the focus group consultation, all but one respondent agreed with the views of the Steering Committee. The dissenting respondent felt that in the light of increasing sophistication of financial transactions and growing complexities of the globalised marketplace, there should be a requirement for the listed companies to have individuals with formal professional financial and accounting qualifications on Audit Committees. The Steering Committee notes that the listed companies may need special requirements, but this would be an issue for the SGX to consider.

**Recommendation 1.6**

**The Companies Act should not prescribe the academic or professional qualifications of directors or mandate the training of directors generally.**

***(c) Maximum age for directors***

32 Section 153 of the Companies Act prohibits the appointment of a person of or above 70 years of age as a director of a public company or a subsidiary of a public company unless his appointment or re-appointment is by ordinary resolution passed at an annual general meeting.

33 It is noted that the annual re-election process required under section 153 enables companies to appoint younger directors who are able to serve whilst also inducing the boards of public companies and their subsidiaries to plan for succession and renewal.

34 The Steering Committee considered whether it is necessary to impose a maximum age limit for directors and whether section 153 should be repealed. In the Steering Committee’s opinion, a person’s ability to act as a director of a company is not principally determined by his age. Rather than focusing simplistically and only on age, other factors should be taken into account when considering if a director is contributing or performing well and whether there should be board renewal. This is because today, persons of or above 70 years of age can be capable of doing the job of a director, and are often re-appointed in practice. In any event, the board renewal process is more appropriate and critical for listed companies than unlisted public companies or private companies.

35 During the focus group consultation, the majority of the respondents agreed with the views of the Steering Committee. There were, however, some dissenting views that the imposition of a maximum age limit still serves a useful function. From a practical standpoint, some respondents felt that although the contribution by a director does not depend solely on his age, having a maximum age limit for directors will encourage companies to consciously review and renew board members so as to promote the effectiveness of the board.

36 After considering all the views received, the Steering Committee recommends that the Companies Act should not impose any maximum age limit for directors and section 153

should be repealed.[14] There is no age limit for directors in the companies legislation of the UK, Australia, New Zealand, Hong Kong, British Columbia and Delaware.

**Recommendation 1.7**

**It is not necessary to impose a maximum age limit for directors in the Companies Act.**

**Recommendation 1.8**

**Section 153 of the Companies Act should be repealed.**

## V. DISQUALIFICATION OF DIRECTORS ON CONVICTION OF OFFENCES INVOLVING FRAUD OR DISHONESTY

37 Where a person is convicted (whether in Singapore or elsewhere) of an offence involving fraud or dishonesty punishable with imprisonment for 3 months or more, he is disqualified under section 154 of the Companies Act from acting as a director of a company or from taking part in the management of the company. This is an automatic disqualification for 5 years as there is no requirement for a disqualification order to be made by the court.

38 It is noted that section 154 provides for two types of disqualification where a director is convicted of an offence: automatic disqualification and disqualification by court order. A distinction is drawn between a conviction of offences involving fraud or dishonesty on the one hand and a conviction of offences involving the formation or management of a company on the other hand.[15] The former attracts automatic disqualification while the latter is subject to disqualification by court order (disqualification order).[16]

39 It is further noted that section 154(6), which allows a director to apply to the High Court for leave to act as a director or take part in the management of the company, applies only to a director against whom a disqualification order has been made. Thus, a director who is automatically disqualified is not able to apply to the High Court for leave.

40 The Steering Committee considered whether the disqualification regime for conviction of offences involving fraud or dishonesty should be an automatic disqualification regime or a disqualification order regime.

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[14] However, for the listed companies, if the SGX decides that an age limit is necessary, an age limit for directors can be imposed in the Listing Manual.

[15] Prior to 1993, section 154 had made no distinction between convictions for offences involving fraud or dishonesty and those involving the formation or management of a company. Both types of conviction had attracted automatic disqualification for a period of 5 years. With the amendments to section 154 in 1993 (Act 22 of 1993), a distinction is now drawn between the two types of conviction.

[16] Australia has a regime similar to Singapore's and provides for automatic disqualification of directors convicted of offences involving dishonesty. However, in the UK and Hong Kong, directors convicted for offences involving dishonesty are not disqualified automatically but by way of a court order. In New Zealand, disqualification can be automatic or by court order.

41 In a disqualification order regime, the court will have to consciously impose disqualification and this will not only be for the offences under the Companies Act, but also for appropriate offences under the Penal Code and other written laws. In contrast, in an automatic disqualification regime, it would be for the director concerned to determine whether or not the offence which he is convicted of is one that involves fraud or dishonesty.

42 A disqualification order regime has the advantage of providing certainty to directors and to companies. However, a difficulty with such a regime is that offences involving fraud or dishonesty are not confined to the offences under the Companies Act, and the onus is on the court to disqualify the offender from acting as a company director. The court may not make the disqualification order as the sentencing judge may not have in mind the relevance of the offence to the role of a company director or may not know that the offender is a company director. If the court did not address its mind to the issue of disqualification or if the issue of disqualification was not raised to the court, resulting in the court not making the disqualification order against the director, it would be too late to raise the issue of disqualification thereafter.

43 Such difficulty would not arise in an automatic disqualification regime as no court order is necessary. A further advantage of an automatic disqualification regime is that offences of fraud or dishonesty committed outside Singapore would also attract automatic disqualification. In such cases, the Singapore court does not need to make a disqualification order.[17]

44 However, there appears to be uncertainty as to what offences would amount to offences involving fraud or dishonesty. The concept of fraud or dishonesty is wide and not connected with the management or formation of a company. There is nothing in the statutory provisions that defines dishonesty in relation to companies. There have been cases where directors are not sure whether the offence which they are convicted of is one involving fraud or dishonesty, and thus are not certain as to whether they become automatically disqualified from acting as a director or from taking part in the management of the company.

45 This uncertainty was highlighted by the District Court in *PP v Foo Jong Kan*[18], where the sentencing judge concluded that as he did not have the appropriate power or jurisdiction to determine whether the automatic disqualification in section 154(1) of the Companies Act applied, he could not determine the meaning of "fraud or dishonesty" in section 154(1). The learned judge stated:

> "42. … As s 154(1) is triggered when the offence is one of fraud or dishonesty, it would seem appropriate that a determination whether such an offence is committed should be made by the sentencing court. Certainly aside from clear cases particularly those in the Penal Code which require dishonesty as an element of the offence, there may be other offences, including possibly the present one[19], in which the situation is less clear, and the matter may call for determination one way or another.

[17] In a disqualification order regime on the other hand, where directors are convicted of offences overseas, the court may have to review overseas findings of fraud or dishonesty. Other jurisdictions may have different criteria on what constitutes fraud or dishonesty.
[18] [2005] SGDC 248.
[19] In *PP v Foo Jong Kan*, Foo Jong Kan, a director, was convicted of a market manipulation offence under section 97(1) of the Securities Industry Act. He caused a misleading appearance as to the price of securities in a

> 43. … [U]pon further consideration of the language of the statute, and the scheme as actually created by the legislature, I concluded that the statute does not in fact contemplate any such determination by the sentencing court.
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> ……
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> 46. Though I was initially concerned that this may cause prejudice or uncertainty for accused persons where there is some difference in reasonable views as to whether an offence involved fraud or dishonesty, and therefore merited determination by the sentencing court, I could not in light of the clear express difference in treatment laid out in s 154, read into sub-section (1) words requiring a determination by the Court."

46 The Steering Committee noted that notwithstanding that legislation such as the Companies Act, Securities and Futures Act and Prevention of Corruption Act are silent on what offences amount to offences involving fraud or dishonesty, the director concerned can always apply to the court for a declaration if there is uncertainty as to whether the offence he is convicted of attracts disqualification. Such an application may be made by originating summons. However, until the declaration is made by the court, the director would potentially be in contravention of section 154(1) during the intervening period between his conviction and the court declaration.

47 The Steering Committee had extensive discussions on the issue and was divided on whether to retain the automatic disqualification regime or move to a disqualification order regime. The Steering Committee considered two options in relation to convictions for offences involving fraud or dishonesty:

(a) Retain the automatic disqualification regime, but allow a disqualified director to apply to the High Court under section 154(6) for leave to act as a director or take part in the management of the company; or

(b) Move to a disqualification order regime.

48 In the UK and Hong Kong[20], directors convicted of offences involving dishonesty are not disqualified automatically, but by way of a court order. Australia provides for automatic disqualification of directors convicted of offences involving dishonesty, but the Australian court may grant leave to a disqualified person who is automatically disqualified.[21] In New Zealand, disqualification can be automatic or by court order.[22]

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public listed company by arranging for buy and sell orders in the securities to be placed near the market closing time at a specified price and volume, with the intention of deflating the closing price of the securities.

[20] In the Hong Kong Companies Ordinance, the court may make a disqualification order under section 168E against a person convicted of an indictable offence which necessarily involves a finding that he acted fraudulently or dishonestly. The effect of the disqualification order is that the person shall not be a director of a company or take part in the promotion, formation or management of a company without leave of the court (section 168D). The Hong Kong provisions are based on the UK Company Directors Disqualification Act 1986.

[21] In Australia, conviction of an offence involving dishonesty and punishable with imprisonment for at least 3 months attracts automatic disqualification under section 206B of the Corporations Act 2001. Under section 206G, the court may grant leave to a disqualified person who is automatically disqualified under section 206B.

[22] In the New Zealand Companies Act 1993, if a person has been convicted of any crime involving dishonesty, he can be disqualified automatically for 5 years unless he first obtains the leave of the court (section 382), or be

49 During the focus group consultation, the majority of the respondents expressed support for option (a)[23], but there was a significant minority who felt that automatic disqualification is too drastic[24]. Further, there were calls for clarity and guidance on what offences would constitute offences involving fraud or dishonesty. In this connection, the Steering Committee received suggestions to provide in the Companies Act a non-exhaustive list of offences involving fraud or dishonesty which would attract automatic disqualification, or to provide in the Companies Act an explanatory description of offences involving fraud or dishonesty with a non-exhaustive list of illustrations, or to provide in the Companies Act or subsidiary legislation the guiding principles that the court shall have regard to when deciding on an application for leave under section 154.

50 The Steering Committee considered all the feedback received and recommends retaining the automatic disqualification regime, but to allow disqualified directors to apply to the High Court for leave to act as a director or take part in the management of the company (option (a)). Although the Steering Committee is of the view that it would not be practicable to draw up a list of offences which conviction would attract automatic disqualification, it was noted that provision of further clarification would be useful. However, further discussion would be needed to ascertain how to clarify which offences would attract automatic disqualification. Options for consideration include stipulating a threshold of minimum fine or term of imprisonment.

**Recommendation 1.9**

**The automatic disqualification regime for directors convicted of offences involving fraud or dishonesty should be retained in the Companies Act, and directors so disqualified should be allowed to apply to the High Court for leave to act as a director or take part in the management of the company.**

## VI. VACATION OF OFFICE AND REMOVAL OF DIRECTORS

### *(a) Resignation of directors*

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disqualified by the court for up to 10 years unless he obtains the leave of the court (section 383), to be a director or take part in the management of a company.

[23] The reasons cited by the majority expressing support for retaining the automatic disqualification regime included the following:

(a) A conviction of fraud or dishonesty reflects lack of integrity, thus such directors should be automatically disqualified.
(b) An automatic disqualification regime saves the courts time and is administratively simpler. Allowing disqualified directors to apply to the court for leave will ensure that aggrieved directors are given a fair hearing.
(c) A disqualification order regime is disproportionately burdensome on the courts, especially in the review of overseas findings of fraud or dishonesty. The onus should remain with the individual.
(d) Any person agreeing to serve as a director should be cognisant of potential disqualification when he signs the consent. It is incumbent on him to seek appropriate legal advice.

[24] The minority opined that most directors are not legally trained and may not be aware of automatic disqualification, thus inadvertently commit an offence by continuing to act as director. It was felt that the burden should be on the prosecution who has resources and systems in place to identify directors who should be subject to disqualification and apply to the court accordingly.

51 The Companies Act does not prescribe the formalities for the resignation of directors. The manner in which a director can resign from his office will be provided for in the company's articles. Article 72(f) of Table A provides that the office of director shall become vacant if he resigns his office by notice in writing to the company. At common law, unless the director's contract or the articles of association require it, a director's resignation need not be accepted by the company.[25] Thus, in practice, a director can resign by simply giving notice to the company and the company need not accept the director's resignation.

52 The Steering Committee considered whether for clarity, the Companies Act should expressly provide that unless otherwise provided by the company's articles, a director may resign by giving the company written notice of his resignation. This would be consistent with the position in Australia[26], New Zealand[27] and Hong Kong[28].

53 During the focus group consultation, most of the respondents were in favour of having such an express provision in the Companies Act. There was, however, a view that there was no need for such provision in the Companies Act as it is a given that a director may resign by giving the company written notice.

54 Having considered all the feedback received, the Steering Committee recommends that the Companies Act expressly provides that unless otherwise provided by the company's articles, a director may resign by giving the company written notice of his resignation.

55 The Steering Committee further considered whether the Companies Act should make it clear that a director's resignation should not be conditional upon the company accepting it. Such a provision should, however, still be subject to the rule on "the last man standing" in section 145(5) which provides that a director shall not resign unless there is remaining in the company at least one director who is ordinarily resident in Singapore. Any purported resignation in breach of section 145(5) will be deemed invalid.

56 During the focus group consultation, most respondents were in favour of having an express provision in the Companies Act that subject to the rule on "the last man standing" in section 145(5), the effectiveness of a director's resignation shall not be conditional upon the company's acceptance. The Steering Committee therefore recommends having such express provision.

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[25] *Walter Woon on Company Law*, 3rd Ed, 2005, at paragraph 7.76.

[26] Section 203A of the Australia Corporations Act 2001 provides that a director may resign by giving a written notice of resignation to the company at its registered office. This is a replaceable rule.

[27] Section 157(2) of the New Zealand Companies Act 1993 provides that a director may resign by signing a written notice of resignation and delivering it to the address for service of the company. The notice is effective when it is received at that address or at a later time specified in the notice. Section 157(1)(a) provides that the office of director of a company is vacated if the person holding that office resigns in accordance with section 157(2).

[28] Section 157D of the Hong Kong Companies Ordinance permits a director to resign from the position of director unless the articles of association provide otherwise or unless there is an agreement between the company and the director which provides otherwise. Notification of such resignation must be given to the Registrar in the specified form, unless the person resigning reasonably believes that the company will not give such notice, in which event that person must give the notice. Where the articles or any agreement with the company requires notice to be given by the resigning director, the resignation will not have effect unless notice of the resignation is given in writing in accordance with such requirement or by sending it by post to, or by leaving it at, the registered office of the company.

**Recommendation 1.10**

**The Companies Act should expressly provide that unless the articles state otherwise, a director may resign by giving the company written notice of his resignation.**

**Recommendation 1.11**

**The Companies Act should expressly provide that subject to section 145(5), the effectiveness of a director's resignation shall not be conditional upon the company's acceptance.**

***(b) Retirement of directors***

57 The Companies Act does not mandate the retirement of directors. Retirement of directors in rotation is usually provided for in the company's articles.[29]

58 The present position is consistent with that in the UK, Australia, New Zealand and Hong Kong.

59 The Steering Committee considered but does not find it necessary for the Companies Act to mandate the retirement of directors.

60 During the focus group consultation, most of the respondents agreed with the view of the Steering Committee. The Steering Committee recommends that it would not be necessary for the Companies Act to mandate the retirement of directors.

**Recommendation 1.12**

**It is not necessary for the Companies Act to mandate the retirement of directors.**

***(c) Removal of directors***

61 Section 152 of the Companies Act provides for the removal of a director of a public company by ordinary resolution, notwithstanding anything in the company's memorandum or articles or in any agreement between the company and the director.

62 The Companies Act, however, does not provide for the removal of a director of a private company. This is left to the company's articles. Article 69 of Table A provides that the company may by ordinary resolution remove any director before the expiration of his period of office, and may by ordinary resolution appoint any person in his stead.[30]

[29] *Walter Woon on Company Law*, 3rd Ed, 2005, at paragraph 7.80. See for example, Table A articles 63 to 66.
[30] If the company's articles are silent on the issue and Table A is excluded, the directors of a private company will be irremovable unless the articles are suitably amended.

63 The Steering Committee considered whether it would be useful if the Companies Act provides for the removal of directors of both private companies and public companies. However, in the case of private companies, the removal of directors should be subject to the companies' articles which can provide for entrenchment. This would give companies flexibility on the issue of entrenchment. In the case of public companies which include listed companies, there should not be entrenchment of directors, as recognised in section 152[31].

64 The Steering Committee noted that the companies legislation of the UK, Australia and New Zealand makes provision for the removal of directors of all types of companies. However, the position on entrenchment of directors in these jurisdictions varies.

65 In the UK, entrenchment of directors is not allowed. Section 168 of the UK Companies Act 2006 provides that a company may by ordinary resolution at a meeting remove a director before the expiration of his period of office, notwithstanding anything in any agreement between the company and the director. However, a director has a right to protest against removal under section 169.

66 In Australia, it is possible for the directors of a proprietary company to be entrenched, but the directors of a public company cannot be entrenched. Section 203C of the Australia Corporations Act 2001 provides for the removal of a director of a proprietary company by resolution, and this is a replaceable rule. On the other hand, section 203D provides that a public company may by resolution remove a director from office despite anything in the company's constitution, any agreement between the company and the director, or any agreement between any or all the members of the company and the director. Section 203D is not a replaceable rule.

67 In New Zealand, it is possible to entrench the directors of any company. Section 156 of the New Zealand Companies Act 1993 provides that subject to the constitution of a company, a director may be removed from office by ordinary resolution passed at a general meeting. This applies to all companies.

68 During the focus group consultation, there was unanimous agreement that it would be useful to provide in the Companies Act that a private company may by ordinary resolution remove any director, subject to contrary provision in the articles. The Steering Committee recommends that the Companies Act expressly provide so.

**Recommendation 1.13**

**The Companies Act should expressly provide that a private company may by ordinary resolution remove any director, subject to contrary provision in the articles.**

[31] Under section 152, special notice must be given of any resolution to remove a director (at least 28 days before the meeting). The director who is to be removed is entitled to make representations in writing to the company and has a right to be heard in his defence. If the director in question was appointed to represent the interests of any particular class of shareholders or debenture holders, the resolution to remove him will not take effect until his successor is appointed.

## VII. PAYMENT OF COMPENSATION TO DIRECTORS FOR LOSS OF OFFICE

69 Section 168(1)(a) of the Companies Act requires any payment of compensation to a director for loss of office as an officer of the company, or any payment as consideration for or in connection with his retirement from such office, to have been disclosed to and approved by the shareholders of the company, otherwise the payment would not be lawful.

70 Section 168(1)(a) speaks of compensation for loss of office as an officer, not as a director. On the basis of the definition of "officer" under section 4(1), it would appear that any payment to a director for loss of office or retirement as executive director must have been disclosed to and approved by the shareholders. Thus, if a director resigns as managing director or executive director but remains a director, any payment of compensation to him must be disclosed to and approved by the shareholders.

71 The Steering Committee considered whether to remove the requirement for shareholders' approval in the case of payment of compensation to executive directors for loss of employment.

72 One view is that a distinction should be drawn between loss of office as a director and termination of employment of an executive director. Compensation for loss of office as a director should be for the shareholders to decide because the shareholders appoint the directors. However, if the payment is to an executive director as an employee, then it should be for the board of directors to decide as employees are appointed by the board. Such a distinction is critical especially in the case of a person who wears both the hats of director and employee.[32]

73 On the other hand, it would not be good corporate governance for executive directors to make payment to themselves without the shareholders' approval. However, the Steering Committee noted that the existing law does allow for payments for loss of office to executive directors to be avoided if the payment is approved in breach of the board's fiduciary duties to the company. In *Lim Koei Ing v Pan Asia Shipyard and Engineering Co Pte Ltd*[33], the court disallowed a payment of damages for premature termination of a contract of service to an executive director, even though the payment had been approved by the board. Although the contract between the director and the company allowed for substantial liquidated damages upon loss of office, the payment was disallowed because it was made in breach of the directors' fiduciary duties. The plaintiff's contract of service was voidable at the instance of the company, as it had been obtained in breach of the directors' fiduciary duties.

74 The Steering Committee was divided in its views on the issue. The focus group feedback on this issue was also split.

75 The reasons given for retaining the requirement for shareholders' approval were as follows:

(a) There is a risk that by removing shareholders' approval for such payments, an additional check on the board will be lost.

[32] Where a person is both a director and an employee, the Steering Committee had noted that in most cases, it would be the loss of employment, rather than the loss of the office of director, that would be in issue. Typically, an employee who is also a director does not draw any fees in his capacity as director.
[33] [1995] 1 SLR 499.

(b) Amending the law to obviate the need for shareholders' approval for terminating a director's employment contract would be a step backwards in corporate governance.

(c) An employee who is also a director does not normally draw any fees in his capacity as director. Thus, if he leaves the company, it is unlikely that he will be paid large compensation for loss of office as director. Any significant compensation would more likely be in relation to his termination of employment. From a corporate governance perspective, it would be incongruous to require shareholders' approval for smaller compensation for loss of office as director but not larger compensation for loss of employment.

76 The reasons against retention of the requirement for shareholders' approval were as follows:

(a) Many companies, when entering into employment contracts with their executive directors, would agree with those directors on certain terms of compensation, including compensation on termination of employment. If such terms have to be approved by the shareholders, the companies would be in breach of their obligations under the employment agreements if the shareholders subsequently do not approve of the terms.

(b) Removing the requirement for shareholders' approval would eliminate the difficulties currently faced by having to differentiate when a payment is for "loss of office" and when it is for "past services", and grappling with issues relating to the existing exceptions in section 168(5).

(c) It is burdensome and administratively costly to convene an EGM to remove a non-performing executive director when his contract of employment is terminated.

77 Having considered all the views, the Steering Committee's recommendation is to retain the requirement for shareholders' approval in section 168(1).

78 It is noted that shareholders' approval for payment of compensation to executive directors is not required in New Zealand, where the board may, subject to restrictions contained in the company's constitution, authorise a payment to a director of compensation for loss of office, if the board is satisfied that to do so is fair to the company.[34] However, shareholders' approval for payment of compensation to executive directors is required in the UK and Australia.

79 In the UK, any payment to a director for loss of office, whether as director or any other office or employment in connection with the management of the affairs of the company, would generally require approval by a resolution of the members.[35] The exceptions are for

[34] New Zealand Companies Act 1993, section 161. No distinction is made between payment of compensation for loss of office as director and loss of office in an executive capacity.

[35] UK Companies Act 2006, sections 215 and 217. This replaces section 312 of the UK Companies Act 1985, which provided that it is not lawful for a company to make to a director of the company any payment by way of compensation for loss of office, or as consideration for or in connection with his retirement from office, without particulars of the proposed payment (including its amount) being disclosed to members of the company and the proposal being approved by the company.

payments made in discharge of legal obligations, payments made by way of damages for breach of legal obligations, payments made by way of settlement or compromise of any claim arising in connection with the termination of office or employment, payments made by way of pension in respect of past services and small payments.[36]

80 In Australia, the giving of benefits in connection with a person's retirement from a board or managerial office in a company generally requires members' approval by resolution passed at general meeting, where the benefit is given by way of compensation for or in connection with the loss of office, or the benefit is given in connection with the retirement from the office.[37] The exceptions are retirement benefits made in respect of leave of absence to which the person is entitled to under an industrial instrument, benefits given under a court order, benefits given in prescribed circumstances, genuine payment by way of damages for breach of contract (subject to a payment limit), benefits given under an agreement made before the person became the holder of the office (subject to a payment limit), and benefits for past services (subject to a payment limit).[38]

81 The Steering Committee further considered whether it would be desirable to introduce a new exception to the requirement for shareholders' approval for payment of compensation to an executive director not exceeding a certain limit. It is noted that the UK has an exception for small payments, while the exceptions in Australia are subject to a payment limit which is tied to the annual base salary of the director. In Singapore, there is an existing exception for bona fide payments in respect of past services not exceeding 3 years' total emoluments of the director in section 168(5)(d) of the Companies Act.

82 The Steering Committee agreed in-principle to introduce a new exception to exempt payment of compensation to executive directors for loss of employment where the payment does not exceed a certain payment limit. For such payments, although shareholders' approval will not be required, disclosure to shareholders will still be necessary.

83 However, the Steering Committee had differing views on the appropriate payment limit. The Steering Committee considered whether it would be appropriate for the payment limit to be tied to the total emoluments of the executive director in the 3 years preceding his termination of employment, as in the existing exception for bona fide payments in respect of past services not exceeding 3 years' total emoluments of the director in section 168(5)(d) of the Companies Act. In other words, where the value or amount of compensation to an executive director does not exceed his total emoluments in the 3 years immediately preceding his termination of employment, shareholders' approval need not be obtained.

84 However, it was felt that capping the compensation not requiring shareholders' approval to the total emoluments of the director in the 3 years prior to his loss of office may result in uncertainty as to the actual capped amount and be subject to abuse. Further, the definition of "emoluments" in the Companies Act is significantly broad and not only covers a director's base salary, allowances and perquisites, but also payments made or consideration given to a director whether made to him in his capacity as a director or otherwise, as long as it is in connection with the affairs of the company.

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[36] UK Companies Act 2006, sections 220 and 221.
[37] Australia Corporations Act 2001, sections 200A, 200B and 200E.
[38] Australia Corporations Act 2001, sections 200F and 200G.

85 The Steering Committee also considered stipulating a payment limit which is tied to the base salary of the executive director and would prefer this approach[39]. In this respect, the Steering Committee's view is that it would be appropriate to exempt payment of compensation to an executive director for loss of office where such compensation does not exceed his base salary for the 3 years immediately preceding his termination. The Steering Committee is of the opinion that a cap based on his base salary for the past 3 years would be reasonable, given that section 168(5)(d) provides a cap for bona fide payments in respect of past services based on a director's total emoluments in the 3 years immediately preceding his retirement or death.

86 The Steering Committee considered whether the payment limit in Australia that is tied to the one-year annual base salary would be suitable, but is of the view that it may be too low. The base salary in Australia is much higher than that in Singapore as the tax rate there is higher. Hence, the base salary quoted in Australia takes that factor into consideration.

**<u>Recommendation 1.14</u>**

**The requirement in section 168 for shareholders' approval for payment of compensation to directors for loss of office should be retained.**

**<u>Recommendation 1.15</u>**

**A new exception should be introduced in the Companies Act to obviate the need for shareholders' approval where the payment of compensation to an executive director for termination of employment is of an amount not exceeding his base salary for the 3 years immediately preceding his termination of employment. For such payment, disclosure to shareholders would still be necessary.**

## VIII. LOANS TO DIRECTORS AND CONNECTED COMPANIES

### *(a) New exceptions to prohibition of loan or giving of guarantee or security*

87 Section 162 of the Companies Act prohibits a company from making a loan to its directors or to directors of related corporations, or to the directors' spouse or children, or giving a guarantee or security in connection with such a loan. To avoid the possibility of a company's directors circumventing section 162 by simply making loans to a company which they control, section 163 prohibits a company from making loans or giving of guarantee or security to connected persons. Both sections 162 and 163 contain exceptions.

88 Under section 163, a company (the lending company) may not make a loan or give a guarantee or security for a loan to another company (the borrowing company) if the directors of the lending company have an interest in 20% or more of the shares of the borrowing

[39] It was noted that as a significant portion of an executive director's emoluments is performance-based, his total annual emoluments tend to vary from year to year. Further, there is the difficulty of determining what goes into an executive director's total annual emoluments, given that many companies have share-based incentives that vest over time (more than one year) and which also have claw-back provisions. An executive director's base salary, on the other hand, is more certain.

company. Interest in shares means either ownership or control over the shares. This prohibition also applies where the borrowing company is incorporated outside Singapore. An interest of a member of a director's family is to be treated as the director's interest. For the purposes of the section, the words "a member of a director's family" include his spouse and children.

89 The Steering Committee received industry feedback that section 163 has caused problems in practice for companies incorporated in Singapore, particularly in joint venture situations. For example, where a company (Company A) enters into a joint venture with another company in which one of Company A's directors has a 20% or more share interest, Company A is prohibited under section 163 from giving a loan or corporate guarantee or security in connection with a loan to the joint venture company. The Steering Committee considered whether to adjust the share interest threshold of 20%, but decided to retain this threshold in the light of the feedback received during the focus group consultation.

90 During the focus group consultation, the Steering Committee received a further proposal to achieve parity of treatment between Singapore companies and foreign companies in relation to section 163. There was feedback that companies incorporated in Singapore are subject to the prohibition in section 163, but the prohibition does not apply to foreign companies listed on the Singapore Exchange. Such disparity has caused difficulty in practice.

91 The Steering Committee is agreeable to the proposal by the focus group to introduce two new exceptions to the prohibition in section 163, as follows:

(a) to allow for loans or guarantee/security to be given to the extent of the proportionate equity shareholding held in the borrower by the directors of the lender/security provider;

(b) where there is prior shareholders' approval (with the interested director abstaining from voting) for the loan, guarantee or security to be given.

**<u>Recommendation 1.16</u>**

**The share interest threshold of 20% in section 163 should be retained.**

**<u>Recommendation 1.17</u>**

**The following two new exceptions to the prohibition in section 163 should be introduced:**

**(a) to allow for loans or security/guarantee to be given to the extent of the proportionate equity shareholding held in the borrower by the directors of the lender/security provider;**

**(b) where there is prior shareholders' approval (with the interested director abstaining from voting) for the loan, guarantee or security to be given.**

### *(b) Extension to quasi-loans and credit transactions*

92 The Steering Committee considered and agreed with a proposal that other than loans, the regulatory regime in sections 162 and 163 should cover quasi-loans, credit transactions and related arrangements. This is because over time, many new types of financial instruments and arrangements have developed. Singapore should update its regulatory regime to keep pace with the changing business environment and to remain on par with leading jurisdictions.

93 In the UK, the regulatory regime for loans is a disclosure and approval regime, rather than a prohibitive regime. Members' approval is required for the making of loans to directors.[40] This requirement extends to quasi-loans[41] and credit transactions[42] in the case of public companies and companies associated with public companies, and also to related arrangements[43].

94 In Australia, members' approval is required for the giving of financial benefits by public companies to their related parties[44]. This is provided in section 208 of the Australia Corporations Act 2001. The "giving of financial benefit" is given a broad interpretation. Section 229 states that the economic and commercial substance of conduct is to prevail over its legal form, and any consideration given for the benefit is to be disregarded. The section cites some examples of giving a financial benefit to a related party, namely, giving or providing the related party finance or property, buying an asset from or selling an asset to the related party, leasing an asset from or to the related party, supplying services to or receiving services from the related party, issuing securities or granting an option to the related party, and taking up or releasing an obligation of the related party.

95 During the focus group consultation, there was unanimous agreement to extend the regulatory regime in the Singapore Companies Act to quasi-loans, credit transactions and related arrangements. There was feedback that there is no limit to creativity in financial

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[40] Section 197 of the UK Companies Act 2006.

[41] A "quasi-loan" (which applies in respect of public companies and associated companies) is defined in section 199 of the UK Companies Act 2006 to mean a transaction under which one party ("the creditor") agrees to pay, or pays otherwise than in pursuance of an agreement, a sum for another ("the borrower") or agrees to reimburse, or reimburses otherwise than in pursuance of an agreement, expenditure incurred by another party for another ("the borrower") —

(a) on terms that the borrower will reimburse the creditor, or
(b) in circumstances giving rise to a liability on the borrower to reimburse the creditor.

[42] A "credit transaction" (which applies in respect of public companies and associated companies) is defined in section 202 of the UK Companies Act 2006 to mean a transaction under which one party ("the creditor") —

(a) supplies any goods or sells any land under a hire-purchase agreement or a conditional sale agreement,
(b) leases or hires any land or goods in return for periodical payments, or
(c) otherwise disposes of land or supplies goods or services on the understanding that payment (whether in a lump sum or instalments or by way of periodical payments or otherwise) is to be deferred.

[43] Pursuant to section 203 of the UK Companies Act 2006, a related arrangement is an arrangement under which another person enters into a transaction that, if it had been entered into by the company, would have required approval under section 197, 198, 200 or 201 and that person, in pursuance of the arrangement, obtains a benefit from the company or a body corporate associated with it. A related arrangement is also one where there is assignment to the company or assumption by the company of any rights, obligations or liabilities under a transaction that, if it had been entered into by the company, would have required approval under section 197, 198, 200 or 201.

[44] The term "related parties" in relation to a public company is defined in section 228 of the Australia Corporations Act 2001. Amongst others, it covers the directors, their spouses, parents and children. It also covers an entity that controls a public company and entities controlled by other related parties.

arrangements and the regime in Singapore should be updated to address the use of devices other than loans.

**Recommendation 1.18**

**The regulatory regime for loans should be extended to quasi-loans, credit transactions and related arrangements.**

## IX. SUPERVISORY ROLE OF DIRECTORS

96 Section 157A(1) of the Companies Act provides that the business of a company shall be managed by or under the direction of the directors. Section 157A was a new provision introduced in 2003 to give effect to a recommendation of the Company Legislation and Regulatory Framework Committee (CLRFC)[45]. It is based on section 198A of the Australia Corporations Act 2001[46].

97 In practice, there is a distinction between the duties performed by the board of directors as a whole and the duties of the management. The board of directors plays a supervisory role rather than manages or gives direction to the company. It is the management that runs the operations of the company. This is especially the case for the larger companies and listed companies. The Steering Committee considered whether section 157A could be improved to recognise and provide for the supervisory powers of the board of directors. This will better reflect the powers and responsibilities of the board of directors.

98 The Steering Committee finds the equivalent provision in the New Zealand Companies Act 1993 to be clear and comprehensive. Section 128 of the New Zealand Companies Act 1993 states:

> Section 128
>
> (1) The business and affairs of a company must be managed by, <u>or under the direction or supervision of,</u> the board of the company. *[emphasis added]*
>
> (2) The board of a company has all the powers necessary for managing, and for directing and supervising the management of, the business and affairs of the company.

[45] According to the Explanatory Statement to the Companies (Amendment) Bill 2003 (Bill No. 3 of 2003), a new section 157A is inserted to give effect (together with the Fourth Schedule as amended) to Recommendation 3.15 of the CLRFC for the enactment of a statutory re-statement of the nature and extent of the powers of directors. As stated in the Final Report of the CLRFC at paragraph 4.7.1, the CLRFC had recommended the adoption of the statutory restatement of the distribution of powers between directors and general meeting following the model used in section 198A of the Australia Corporations Act 2001 to override Article 73 of Table A in the Fourth Schedule which had provided that management powers are also subject to "such regulations, being not inconsistent with the aforesaid Regulations or provisions, as may be prescribed by the company in general meeting."

[46] Section 198A(1) of the Australia Corporations Act 2001 states that "the business of a company is to be managed by or under the direction of the directors".

(3) Subsections (1) and (2) are subject to any modifications, exceptions, or limitations contained in this Act or in the company's constitution.

99 During the focus group consultation, the majority of the respondents agreed with the Steering Committee's view to amend section 157A to provide that the business of a company shall be managed by, or under the direction or supervision of, the directors.

**Recommendation 1.19**

**Section 157A(1) of the Companies Act should be amended to provide that the business of a company shall be managed by, or under the direction or supervision of, the directors.**

## X. POWER OF DIRECTORS TO BIND THE COMPANY

100 Section 23 of the Companies Act was introduced in 2004 to confer statutory powers of a natural person on companies. Section 25 was then amended to retain the *ultra vires* doctrine to preserve contractual rights of internal redress by the members against the officers of the company or against the company, where there is a lack of capacity or power by the company to do a purported act. Section 25A (which originated from section 19 of the New Zealand Companies Act 1993) was also introduced at the same time to provide that notwithstanding anything in the memorandum or articles of a company, a person is not deemed to have constructive knowledge of the contents of the memorandum or articles of, or any other document relating to, the company merely because such documents have been registered with ACRA or are available for inspection at the company's registered office address.

101 It has been proposed that it would be helpful to adopt section 40 of the UK Companies Act 2006. Section 40 provides that in favour of a person dealing with a company in good faith, the power of the directors to bind the company, or authorise others to do so, is deemed to be free of any limitation under the company's constitution.[47]

102 Section 40 restates sections 35A and 35B[48] of the UK Companies Act 1985. It is similar but not identical to section 35A. Section 35A was enacted in 1989 to give effect to Article 9.2 of the First Company Law Directive of the European Economic Community

[47] As explained in *Palmer's Company Law Annotated Guide to the Companies Act 2006* at page 84, the intent of section 40 (as was the intent of section 35A of the 1985 Act) is to protect third parties dealing with the company in good faith from any internal restrictions contained in (usually) the articles of association which limited the power of the board to act on the company's behalf. For example, where the articles contained a provision to the effect that contracts over a certain value required the unanimous consent of the board, and a contract of that nature was entered into without unanimous consent, the counterparty could rely on section 35A to enforce the contract against the company as long as he was dealing with the company in good faith. Equally, where the authorisation of another person to act on behalf of the company required, say, unanimous consent of the board, a third party in good faith could rely on the section to "cure" consent defectively delivered.

[48] Section 35B of the UK Companies Act 1985 absolved a person dealing with the company from any duty to enquire as to the existence of limitations on the powers of directors to bind the company or authorise others to do so.

(68/151/EEC)[49]. The effect of section 35A was that a third party dealing with a company in good faith need not concern itself about whether a company is acting within its constitution. It reflected and to some degree extended the "indoor management rule" from *Royal British Bank* v *Turquand* (1856) All E.R. Rep 435. This rule effectively states that a person dealing with a company in good faith is entitled to assume that any internal procedures contained in the company's constitution had been properly complied with.[50]

103 The companies legislation in New Zealand (sections 17 and 19) and Australia (sections 124 and 125) deal with a company's capacity, and do not contain a provision that is identical with section 40 of the UK Companies Act 2006. The closest provision in the New Zealand Companies Act 1993 is section 18, which provides that assertions of lack of authority may not be made for dealings between a company and other persons, unless certain conditions are satisfied.

104 During the focus group consultation, the majority of the respondents were in favour of adopting section 40 of the UK Companies Act 2006. However, there was a view that if a third party has been given express notice that the articles of association of the company limits the board's authority or power to bind the company and the third party then proceeds to enter into a transaction with the company with full knowledge of such limitation, the company should not be held liable for the transaction entered into by the board contrary to such limitation.

105 Having considered all the feedback received, the Steering Committee's recommendation is to provide in the Companies Act that a person dealing with the company in good faith should not be affected by any limitation in the company's articles.

**Recommendation 1.20**

**The Companies Act should provide that a person dealing with the company in good faith should not be affected by any limitation in the company's articles.**

## XI. POWER OF DIRECTORS TO ISSUE SHARES OF COMPANY

106 Section 161 of the Companies Act provides that notwithstanding anything in a company's memorandum or articles, the directors cannot exercise any power of the company to issue shares unless it has been approved by the company in general meeting. In practice, the approval under section 161 is usually given by general mandate, which will expire at the next annual general meeting. However, there can be specific shareholders' approval for a particular issue of shares (not in pursuance of an offer, agreement or option made or granted by the directors when the approval is in force, referred to in section 161(4)[51]), which will

[49] Article 9.2 of the Directive provides that the limits on the powers of the organs of the company, arising under the statutes or a decision of the competent organs, may never be relied on as against third parties, even if they have been disclosed. The board of directors was treated as one of the "organs" of the company.
[50] *Palmer's Company Law Annotated Guide to the Companies Act 2006*, at page 84.
[51] Section 161(4) allows the directors to issue shares notwithstanding that an approval has ceased to be in force if the shares are issued in pursuance of an offer, agreement or option made or granted by them while the approval was in force and they were authorised by the approval to make or grant an offer, agreement or option which would or might require shares to be issued after the expiration of the approval.

lapse at the next annual general meeting under section 161(3) if the approval is not renewed at the next annual general meeting. In such a situation, an issue has arisen as to whether it would be necessary to obtain approval at the annual general meeting if there is already shareholders' approval.

107 The Steering Committee considered and agreed with a proposal to amend section 161 to allow specific shareholders' approval for a particular issue of shares to continue in force notwithstanding that the approval is not renewed at the next annual general meeting, provided that the specific shareholders' approval satisfies certain conditions. The conditions are that the specific shareholders' approval must specify a maximum number of shares that can be issued and that the approval will expire at the end of two years.

108 There is a differing view that the proposed amendment is not necessary as it appears to cater to specific mandate for an issue of shares for a proposed transaction. If the company is not able to ascertain the main terms of the proposed transaction, it would be premature to lay it before the shareholders for the purpose of obtaining their approval for that transaction.

109 However, section 161 currently does not only envisage a specific mandate being obtained for a specific transaction. It is wide enough to cover situations outside the scope of section 161(4) including proposed transactions for which the terms cannot be ascertained at the time the specific shareholders' approval was sought.

**Recommendation 1.21**

**Section 161 of the Companies Act should be amended to allow specific shareholders' approval for a particular issue of shares to continue in force notwithstanding that the approval is not renewed at the next annual general meeting, provided that the specific shareholders' approval specifies a maximum number of shares that can be issued and expires at the end of two years. This does not apply to the situation referred to in section 161(4) for the issue of shares in pursuance of an offer, agreement or option made or granted by the directors while an approval was in force.**

## XII. DIRECTORS' FIDUCIARY DUTIES

### *(a) Codification of directors' fiduciary duties*

110 Section 157(1) of the Companies Act states that a director shall at all times act honestly and use reasonable diligence in the discharge of the duties of his office. Section 157(2) provides that an officer or agent of a company shall not make improper use of any information acquired by virtue of his position as an officer[52] or agent of the company to gain, directly or indirectly, an advantage for himself or for any other person or to cause detriment to the company. This is the statutory statement of a director's duties under the Singapore Companies Act. It is derived from similar provisions in Australian legislation.[53]

[52] By section 4(1), "officer" includes any director.
[53] *Walter Woon on Company Law*, 3rd Edition, 2005, at paragraph 8.6.

111 Section 157 does not purport to be an exhaustive statement of a director's duties. In fact, section 157(4) specifically provides that the section is in addition to and not in derogation of any other rule of law relating to the duty or liability of directors or officers of a company. The effect of section 157 is to render mandatory the duties that it imposes. However, the fiduciary duties under common law are not excluded and continue to apply.[54]

112 In 2006, the following directors' duties were codified in the UK Companies Act 2006[55]:

(a) Duty to act within powers;
(b) Duty to promote the success of the company;
(c) Duty to exercise independent judgment;
(d) Duty to exercise reasonable care, skill and diligence;
(e) Duty to avoid conflicts of interests;
(f) Duty not to accept benefits from third parties;
(g) Duty to declare interests in proposed transaction or arrangement.

113 The Steering Committee considered whether the Singapore Companies Act should adopt the UK approach of codifying the directors' fiduciary duties[56]. In the UK, the statutory duties replace the corresponding common law rules and equitable principles from which they derive, and are to be interpreted in the same way as the common law rules and equitable principles.[57] By this approach, the UK Government sought to balance precision of the statutory statement against the need for continued flexibility and development of the law.[58] However, it remains to be seen whether this intent would be successfully achieved.[59] The Steering Committee received feedback from British academics and practitioners who are ambivalent about the codification of the directors' fiduciary duties in the UK and have expressed reservation about its usefulness.

114 In codifying the directors' fiduciary duties, the UK Government had accepted the recommendations of the Steering Group which led the Company Law Review (CLR) that

[54] *Walter Woon on Company Law*, 3rd Edition, 2005, at paragraph 8.7.
[55] UK Companies Act 2006, sections 171 to 177.
[56] The UK Steering Group which led the Company Law Review (CLR) in its report *Developing the Structure* at chapter 3 set out the following general obligations for directors, as gleaned from case law:

- to comply with the constitution and to use powers under it for proper purposes;
- to run the undertaking for the benefit of the company (i.e. generally speaking for the benefit of its members as a whole) and not for any other purpose;
- to maintain their independence of judgment;
- to avoid profiting personally from their position and to avoid conflicts of interest without the consent of the members or the authority of the constitution;
- to act fairly as between members; and
- to apply reasonable care and skill in exercising all their functions.

[57] Section 170(3) and (4) of the UK Companies Act 2006.
[58] See Explanatory Notes to the UK Companies Act 2006, paragraph 305.
[59] It was noted at paragraph 3.11 of the Hong Kong Government's Second Public Consultation Paper on Companies Ordinance Rewrite (2 April 2008) that there were heated debates in the UK during the process of introducing the statutory statement of directors' duties. While some commentators praised the statement for improving clarity and certainty and striking a good balance between precision and flexibility, others were concerned that the statement created new uncertainties and difficulties. For example, the requirement for directors to take into account various new factors in complying with the duty to promote the success of the company may pose new challenges to directors.

there should be a statutory statement of the directors' general duties and that this, subject to two exceptions[60], should be a codification of the current law. CLR's reasons were as follows:

- "to provide greater clarity on what is expected of directors and make the law more accessible. In particular, they sought to address the key question "in whose interests should companies be run?" in a way which reflects modern business needs and wider expectations of responsible business behaviour;

- to make development of the law in this area more predictable (but without hindering development of the law by the courts);

- to correct what the CLR saw as defects in the present duties relating to conflicts of interest." [61]

115 The Steering Committee accepts that the arguments in favour of codification are ones of certainty and accessibility[62]. It should be noted in this context that the UK did not traditionally have a general statutory statement of a director's duties. The Steering Committee also considered the arguments against codification. The strength of the common law lies in the flexibility of the judges to tailor their decisions according to justice. Fiduciary duties cannot be codified without being stated in detailed terms, in which case there will be a loss of flexibility. Further, attempting to restate in statutory form duties which are not yet well-settled or are still developing might restrict the ability of the law to develop further and adapt to changing circumstances. It should be noted that in contrast to the UK, the Singapore Companies Act has a statutory statement of directors' duties, which is based on an Australian model. The Singapore section does not exclude the common law.

116 The Steering Committee notes that the UK may be the only major jurisdiction which has sought to exhaustively codify directors' fiduciary duties. The Australia Corporations Act 2001 has not codified the directors' duties in the same way as the UK Companies Act 2006. There is a statutory statement of the directors' duties in sections 180 to 183 of the Australia Corporations Act 2001[63], but this is not an exhaustive statement as the statutory duties have effect in addition to the existing common law and equitable principles (section 185).

117 The New Zealand Companies Act 1993 has sought to codify some of the directors' fiduciary duties[64], but it does not appear to have codified as extensively as the UK Companies

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[60] The two exceptions relate to the regulation of conflicts of interest, where the statutory statement departs from the current law. See the Explanatory Notes to the UK Companies Act 2006, paragraph 302.

[61] Explanatory Notes to the UK Companies Act 2006, paragraphs 300 and 301.

[62] On the issue of accessibility, the Steering Committee has considered the possibility of having guidance notes on directors' duties instead. One suggestion was for SGX to issue such guidance notes.

[63] Sections 180 to 183 of the Australia Corporations Act 2001 provide for the following duties:

(a) Duty to exercise powers and discharge duties with care and diligence (section 180);
(b) Duty to exercise powers and discharge duties in good faith in the best interests of the corporation and for a proper purpose (section 181);
(c) Duty not to improperly use his position to gain an advantage or cause detriment to the corporation (section 182);
(d) Duty not to improperly use information by virtue of his position to gain an advantage or cause detriment to the corporation (section 183).

[64] Sections 131 to 138 of the New Zealand Companies Act 1993 provide for the following directors' duties:

(a) Duty to act in good faith and in the best interests of the company (section 131);
(b) Duty to exercise powers for a proper purpose (section 133);

Act 2006. The directors' duty to promote the success of the company for the members' benefit, duty to exercise independent judgment, duty to avoid conflicts of interest, and duty not to accept benefits from third parties, which are codified in the UK Companies Act 2006, have not been similarly codified in the New Zealand Companies Act 1993. Further, the UK Companies Act 2006 contains an express provision that the statutory duties have effect in place of the common law rules and equitable principles as regards the duties owed to a company by a director. The New Zealand Companies Act 1993 does not contain such a provision.

118 Hong Kong has not codified directors' fiduciary duties. During a recent public consultation[65] by the Hong Kong Government, it was found that the idea of codifying directors' duties remained controversial and responses on this issue were highly divided. The Hong Kong Government concluded that it would be premature to have comprehensive codification at this stage and proposed to just have a statutory statement on the directors' duties to exercise care, skill and diligence.[66]

119 After extensive discussions, the Steering Committee is of the view that it would not be desirable to codify the directors' fiduciary duties in the same manner as the UK as this may not be best for business efficacy. It would be preferable to monitor the developments in the UK to ascertain if the codification of the directors' duties there is useful. This is especially since the UK provisions are still new, having come into operation only on 1 October 2007 (for four duties[67]) and 1 October 2008 (for the remaining three duties[68]). At the same time, we should observe the developments in the other leading jurisdictions. If the experiences of other jurisdictions suggest that codifying directors' duties in a similar manner is a positive development, then it may be useful for Singapore to do so.

120 During the focus group consultation, the majority of the respondents expressed agreement with the Steering Committee's view. One respondent, however, felt that codification would provide better guidance for directors on the standards of behavior

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(c) Duty to comply with the Companies Act and the constitution of the company (section 134);
(d) Duty to exercise care, diligence and skill (section 137);
(e) Duty not to allow the company to engage in reckless trading (section 135);
(f) Duty not to agree to the company incurring an obligation unless the director believes at that time on reasonable grounds that the company will be able to perform the obligation when it is required to do so (section 136).

It is noted that prior to 1993, there was no statutory statement of the directors' duties in New Zealand. The New Zealand Companies Act 1955 did not contain any statutory statement of the directors' duties. Instead, the directors' duties had to be gleaned from a large volume of complex case law. In 1987, the New Zealand Law Commission was of the view that the existing law relating to the duties of directors was inaccessible, unclear and extremely difficult to enforce. It recommended a statutory statement of the directors' duties, recognising at the same time that it would be impossible to encapsulate all the current legal principles and unwise to inhibit development of the standards appropriate in particular cases by attempting codification.

[65] Second Public Consultation on Companies Ordinance Rewrite by the Hong Kong Government, issued on 2 April 2008.

[66] First Phase Consultation of the draft Companies Bill by the Hong Kong Government, issued on 17 December 2009.

[67] These are the duty to act within powers, duty to promote the success of the company, duty to exercise independent judgment and duty to exercise reasonable care, skill and diligence under sections 171 to 174 of the UK Companies Act 2006 respectively.

[68] These are the duty to avoid conflicts of interest, duty not to accept benefits from third parties and duty to declare interest in proposed transaction or arrangement under sections 175 to 177 of the UK Companies Act 2006 respectively.

expected of them. There was also feedback that such guidance could be in the form of non-statutory practice directions or guidance notes instead.

<u>**Recommendation 1.22**</u>

**It would not be desirable to exhaustively codify directors' duties. The developments in the UK and other leading jurisdictions should continue to be monitored.**

***(b) Consequences of breach of duties under section 157***

121 Under section 157(3) of the Companies Act, a breach of the provisions in section 157 renders the officer or agent liable both civilly and criminally. He is liable to the company for any profit made by him or for any damage suffered by the company as a result of the breach. Breach of the duties in section 157 is also an offence. If found guilty, the officer or agent is liable to a fine not exceeding $5,000 or to imprisonment for a term not exceeding twelve months.

122 The Steering Committee considered a proposal to decriminalise breach of the duties under section 157. Notwithstanding the position in the other jurisdictions, the Steering Committee found it appropriate to retain the current position in section 157(3) so as not to send the wrong signal. The Steering Committee is concerned that decriminalisation may encourage misconduct.

123 In the UK, breach of the statutory duties of a director under sections 171 to 177 of the UK Companies Act 2006 would not subject the director to criminal liability. The consequences of breach are civil in nature.[69] This is also the position in New Zealand[70].

124 In Australia, a director faces criminal sanction in certain circumstances, namely, for failure to discharge his duty to act in good faith in the best interests of the corporation and for a proper purpose and is reckless or intentionally dishonest, for use of his position dishonestly, and for dishonest use of information obtained because of his position.[71] However, the Australia Corporations Act 2001 provides civil consequences for breach of his duty to exercise care and diligence, duty to exercise good faith in the best interests of the corporation and for a proper purpose, duty not to make improper use of his position and duty not to make improper use of information acquired by virtue of his position.[72]

125 During the focus group consultation, the majority of the respondents were in favour of maintaining the *status quo*. It was opined that the retention of criminal liability serves as a useful deterrent. A few respondents, however, proposed the introduction of a civil penalty regime. In this context, the Steering Committee noted that a civil penalty regime, if

[69] Section 178(1) of the UK Companies Act 2006 provides that the consequences of breach (or threatened breach) of sections 171 to 177 are the same as would apply if the corresponding common law rule or equitable principle applied.
[70] The New Zealand Companies Act 1993 provides a criminal penalty only for breach of the duty to disclose directors' interests under section 140.
[71] Section 184 of the Australia Corporations Act 2001.
[72] These are civil penalty provisions, as stated in a note to sections 180, 181, 182 and 183 of the Australia Corporations Act 2001.

introduced, should apply across the entire Companies Act, and not just in respect of the directors' duties. This issue is currently the subject of a review by ACRA.

**Recommendation 1.23**

**Pending ACRA's review, a breach of the duties in section 157 should still render an officer or agent of a company criminally liable.**

***(c) Extending section 157(2) to cover improper use of position***

126 Section 157(2) of the Companies Act provides that an officer or agent of a company shall not make improper use of any information acquired by virtue of his position as an officer or agent of the company to gain, directly or indirectly, an advantage for himself or for any other person or to cause detriment to the company.

127 The equivalent provision in the Australia Corporations Act 2001 is section 183[73]. In addition, section 182 provides that a director, secretary, other officer or employee of a corporation must not improperly use their position to gain an advantage for himself or someone else, or cause detriment to the corporation.

128 The Steering Committee is of the view that it would be useful to adopt the Australian approach by widening the scope of section 157(2) to extend the prohibition to cover improper use of a person's position as an officer or agent of a company, other than the present prohibition covering improper use of any information acquired by virtue of a person's position as an officer or agent, to gain an advantage for himself or any other person or to cause detriment to the company.

129 During the focus group consultation, the majority of the respondents agreed with the Steering Committee's view. It was felt that the ultimate test is that an individual obtained an unfair advantage through an abuse of his position. It is irrelevant whether it concerns merely information or otherwise. It was also opined that such an extension was a logical one.

**Recommendation 1.24**

**The prohibition in section 157(2) should be extended 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.**

[73] Section 183 of the Australia Corporations Act 2001 provides that a person who obtains information because he is or has been a director or other officer or employee of a corporation must not improperly use the information to gain an advantage for themselves or someone else, or cause detriment to the corporation.

## XIII. IMPOSITION OF LIABILITY ON OTHER OFFICERS

130 Most of the statutory requirements and duties in the Companies Act are imposed on the directors only. However, some provisions, such as section 157(2) prohibiting the improper use of information acquired by virtue of a person's office, impose the requirements on the officers of a company.

131 "Officer" in relation to a corporation is defined under section 4(1) as including "any director or secretary of the corporation or a person employed in an executive capacity by the corporation".

132 The Steering Committee considered whether it would be appropriate to extend certain statutory requirements and duties to the other officers of a company.

### *(a) Extension of disclosure requirements*

133 The Steering Committee considered whether to impose the following disclosure requirements on the other officers of a company, not just the directors:

(a) duty to disclose conflict of interests in transactions or proposed transactions with the company, or by virtue of holding any office or property (section 156);

(b) duty to disclose shareholdings and interests in shareholdings in the company or related corporation and changes thereof (section 165).

134 A contravention of any of these disclosure requirements would attract a criminal penalty.

135 One view is that such disclosure requirements should be imposed on the key management officers of a company employed in an executive capacity as these persons have control and influence over the decisions of the company. The directors do not necessarily run the company. In modern companies, the key decisions are made by the key management officers who may not be directors. It would be necessary to know their conflicts of interests and other interests. The key management officers generally refer to the Chief Executive Officer and the most senior person responsible for the financial affairs of the company. It also does not seem consistent to impose criminal liability on the directors, some or all of whom may not work full-time for the company, but not the key management officers who are full-time employees and who play a critical role in the decision-making of the company.

136 Another view is that it would be adequate to extend the disclosure requirements to the Chief Executive Officer being the person at the apex of the management of the company. It would be too harsh to subject the other officers to criminal liability as well.

137 It is noted that the companies legislation of the UK, Australia, New Zealand and Hong Kong do not impose the duty to disclose interests in transactions on non-directors.

138 In defining who a key management officer is, the Steering Committee finds the definition of "officer" in relation to a corporation under section 9 of the Australia Corporations Act 2001 to be a useful guide, that is, "a person who makes or participates in making decisions that affect the whole or a substantial part of the business of the corporation,

or who has the capacity to affect significantly the corporation's financial standing, or in accordance with whose instructions or wishes the directors of the corporation are accustomed to act[74]".

139 The Steering Committee consulted the focus group on the following three options:

(a) Extension to the Chief Executive Officer only;

(b) Extension to the key management officers, that is, any person who makes or participates in making decisions that affect the whole or a substantial part of the business of the company, or who has the capacity to affect significantly the company's financial standing, or in accordance with whose instructions or wishes the directors of the company are accustomed to act;

(c) Extension to all the officers (this would include any person employed in an executive capacity by the company, as defined in section 4(1) of the Singapore Companies Act).

140 The majority of the respondents supported extension of the disclosure requirements to non-directors. However, there were mixed views as to which officers should be subject to the disclosure requirements. A number of respondents supported extension to the Chief Executive Officer only, while others were in favour of extension to the key management officers such as the Chief Executive Officer and the Chief Financial Officer. None of the respondents were in favour of extending to all the officers of the company.

141 The minority view which disagreed to an extension of the disclosure requirements felt that it would be sufficient to impose such duties on the directors only as the directors are the ultimate overseers of the company. Extension would put an additional onerous responsibility on non-directors, and this would lead to increased costs of compliance. It was also opined that it would be too harsh to impose criminal penalties on other officers for non-disclosure. Such an extension would not be necessary as the officers of a company are already governed by the company's internal policy on code of conduct and ethics which they have to comply as part of their employment contracts. It was further felt that such an extension may impact on the willingness of individuals to assume key management positions of a company.

142 After considering all the feedback received, the Steering Committee recommends extension of the disclosure requirements to the Chief Executive Officer only as he is the person at the apex of the management of the company. The Steering Committee noted that extension to the Chief Executive Officer would be consistent with the Securities and Futures (Amendment) Act 2009 (introducing a new section 133) where the directors and the Chief Executive Officer of any listed company who is not also a director are required to notify the company of their shareholdings and changes in shareholdings.

[74] This excludes advice given by the person in the proper performance of functions attaching to the person's professional capacity or his business relationship with the directors or the corporation.

**<u>Recommendation 1.25</u>**

**The disclosure requirements under sections 156 and 165 should be extended to the Chief Executive Officer of a company.**

***(b) Extension of duty to act honestly and exercise reasonable diligence***

143 In Australia, the duty to exercise reasonable care and diligence and the duty to act in good faith are imposed on both the directors and other officers[75] of a corporation (sections 180 and 181 of the Corporations Act 2001). The UK Companies Act 2006 and New Zealand Companies Act 1993 impose the duty on the directors only.

144 The Steering Committee considered whether it would be timely to extend the duty to act honestly and exercise reasonable diligence in section 157(1) to the other officers of a company, following the Australian approach, as company officers often wield greater control and influence over the company than non-executive directors. It is noted that the duty not to make improper use of information to gain an advantage under section 157(2) is already imposed on the officers and agents of the company.

145 It is noted that the Chief Executive Officer is usually a director of the company and would be caught by section 157(1) as a director. However, as he is the person at the apex of the management, he should also be subject to the duty even if he is not a director. The Steering Committee therefore recommends that the duty to act honestly and exercise reasonable diligence in section 157(1) be extended to the Chief Executive Officer. However, the Steering Committee considered but finds no compelling reason to extend the duty beyond the Chief Executive Officer.

146 During the focus group consultation, the majority of the respondents were in favour of extending the duty only to the Chief Executive Officer. The minority was against such extension as they were concerned that the criminal sanction for breach of the duty should not be extended beyond the directors.

**<u>Recommendation 1.26</u>**

**The duty to act honestly and use reasonable diligence in section 157(1) should be extended to the Chief Executive Officer of a company.**

## XIV. DISCLOSURE OF COMPANY INFORMATION BY NOMINEE DIRECTORS

147 Under section 158 of the Companies Act, a director is permitted to disclose information which he has in his capacity as a director or an employee of a company, being information that would not otherwise be available to him, to a person whose interests the director represents (that is, his nominating shareholder) or a person in accordance with whose

[75] As defined in section 9 of the Australia Corporations Act 2001.

directions or instructions the director may be required or is accustomed to act in relation to the director's powers and duties, if certain conditions are satisfied. The conditions are set out in section 158(3), as follows:

(a) the director declares at a meeting of the directors of the company the name and office or position held by the person to whom the information is to be disclosed and the particulars of such information;

(b) the director is first authorised by the board of directors to make the disclosure; and

(c) the disclosure will not be likely to prejudice the company.

148 During the focus group consultation, the Steering Committee received feedback that on a literal reading, specific approval has to be obtained for each piece of information to be disclosed. This is not practicable and cumbersome.

149 Further, section 158 is capable of having three different interpretations: (a) each and every piece of information must be approved by the board before it could be disclosed; (b) general mandate would be sufficient; and (c) disclosure would be possible as long as it is not detrimental to the company, which is the position under the common law. This makes the application of section 158 unclear.

150 The Steering Committee also received feedback that as a result of the conditions stipulated in section 158(3), there are constraints faced by listed holding companies in Singapore in receiving information from its listed subsidiaries. A listed subsidiary will not be prepared to disclose information to its holding company unless it is prepared to disclose the same information to all its shareholders as well. The board members of the listed subsidiary, including nominee directors representing the holding company generally, will not be comfortable to disclose information to its parent company to avoid incurring personal liability unless such information has been approved by the whole board of the listed subsidiary on which he sits on.

151 As the holding company has to ensure that the entire group is properly run, the holding company would need more information than passive shareholders. As such, the holding company's directors have a heavy responsibility to ensure that all the core businesses and operating units including listed subsidiaries are well managed to produce desirable financial results. For the holding company to receive the information only after release of the announcement by its listed subsidiaries would be too late.

152 It was thus proposed that section 158(3) be reviewed to allow nominee directors representing the holding company on the board of its listed subsidiaries to disclose information concerning the subsidiary to their nominating shareholders without having to satisfy the conditions listed in subsection (3). This will facilitate more efficient management of groups with listed subsidiaries. Any concerns relating to improper use of information is mitigated and governed under the Securities and Futures Act. The protection for insider trading has been provided under the Securities and Futures Act which applies to the management and directors of holding company.

153 Another proposal received by the Steering Committee is to amend section 158 to follow the wording of section 145 of the New Zealand Companies Act 1993, which is

consistent with the common law position. Section 145 of the New Zealand Companies Act 1993 allows the director of a company to disclose information to a person whose interests the director represents (that is, his nominating shareholder), unless it is prohibited by the board.

154 The Steering Committee notes that the New Zealand provision deals not only with disclosure but also with making use of or acting on the information. The Steering Committee is of the view that it would not be necessary to address the latter as this would lead to complications with issues such as insider trading.

155 Having considered the feedback received, the Steering Committee's recommendation is to amend section 158 to enable the board of directors to allow the disclosure, whether by general or specific mandate, subject to the overarching consideration that there should not be any prejudice caused to the company. As the requirement stated in section 158(3)(a) seems to rely on a degree of particularity which may be difficult to satisfy, the Steering Committee also recommends deleting section 158(3)(a) and leaving it to the board to require the details if desired.

**Recommendation 1.27**

**Section 158 of the Companies Act should be amended —**

**(a) to enable the board of directors to allow the disclosure of company information, whether by general or specific mandate, subject to the overarching consideration that there should not be any prejudice caused to the company; and**

**(b) to remove the requirement in section 158(3)(a) for declaration at a meeting of the directors of the name and office or position held by the person to whom the information is to be disclosed and the particulars of such information, but to leave it to the board of directors to require such details if desired.**

## XV. INDEMNITY FOR DIRECTORS

### *(a) Indemnity for claims brought by third parties*

156 Any provision, whether in the articles or in a contract or otherwise, indemnifying a director against any liability for negligence, default, breach of duty or breach of trust in relation to the company is void. This is provided in section 172(1) of the Companies Act. Section 172 applies to officers[76] and auditors of the company, and not just directors.

157 Section 172(2)(b) provides that section 172 does not prevent a company from indemnifying any director against any liability incurred by him: (i) in defending any proceedings (civil or criminal) in which judgment is given in his favour or in which he is

[76] "Officer", in relation to a corporation, is defined in section 4(1) to include any director, secretary or a person employed in an executive capacity by the corporation.

acquitted; or (ii) in connection with any application under section 76A(13) or section 391[77] or any other provision of the Companies Act, in which relief is granted to him by the court.

158 There appears to be some uncertainty as to whether a company is prohibited under section 172 from providing indemnity for claims brought by third parties. The term "in relation to the company" used in the prohibition in section 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.

159 The leading jurisdictions allow companies to indemnify their directors against claims brought by third parties, subject to certain conditions.

160 In the UK Companies Act 2006, section 232(2) prohibits a company from providing an indemnity for a director against any liability attaching to him in connection with any negligence, default, breach of duty or breach of trust in relation to the company. One exception to the prohibition is found in section 234, which allows a company to provide indemnity against liability incurred by the director to a person other than the company or an associated company, provided that the indemnity is not against:

(a) liability to pay a fine imposed in criminal proceedings;

(b) liability to pay a sum payable to a regulatory authority by way of a penalty for non-compliance with a regulatory requirement;

(c) liability incurred in defending criminal proceedings in which he is convicted or civil proceedings in which judgment is brought against him; or

(d) liability in connection with an application for relief in which the court refuses to grant him relief.

161 Section 199A of the Australia Corporations Act 2001 expressly prohibits a company from providing indemnity in respect of a director's liability to a third party except where the liability arises out of conduct in good faith.

162 In the New Zealand Companies Act 1993, section 162 provides that if it is expressly authorised in the constitution of a company, the company may indemnify a director in relation to liabilities he may have to third parties for any act or omission in his capacity as a director.

163 As Singapore companies become more globalised, the risk of them being exposed to liabilities to third parties, for example, arising from the frequent class actions by groups of shareholders in the US, is real and should be addressed. The Steering Committee is of the view that the Companies Act should be amended to expressly allow a company to provide indemnity to its directors for claims brought by third parties.

[77] Section 391 gives the court power to relieve officers of a corporation (which include directors) from the consequences of their negligence, default, breach of duty or breach of trust.

164 During the focus group consultation, the majority of the respondents were in favour of expressly allowing a company to provide indemnity to its directors for claims brought by third parties.

165 The Steering Committee also considered whether it would be desirable to adopt the UK provisions on this issue. There was, however, feedback from the focus group that adoption of the UK provisions may give rise to difficulties. In the circumstances, the Steering Committee recommends that section 172 of the Singapore Companies Act should simply be amended to expressly allow a company to provide indemnity against liability incurred by its directors to third parties, instead of adopting the UK provisions.

**Recommendation 1.28**

**Section 172 of the Companies Act should be amended to expressly allow a company to provide indemnity against liability incurred by its directors to third parties.**

***(b) Indemnity against potential liability***

166 The Steering Committee considered and agreed with a proposal to amend section 172(2)(b) to clarify that a company is allowed to indemnify its directors against potential liability. The proposal is for section 172(2)(b) to cover liability that has been incurred or is to be incurred by the directors. There appears to be some uncertainty as to whether the use of the word "incurred" in section 172(2)(b) is wide enough to cover potential liability. The concern is that the restrictions on a company's power to make loans to its directors have prevented companies from lending money to its directors on a "to be incurred" basis even to pay for his legal expenses.

167 The focus group unanimously agreed with the Steering Committee's view.

**Recommendation 1.29**

**The Companies Act should be amended to clarify that a company is allowed to indemnify its directors against potential liability.**