

# WEEK 4: TOPIC 6: DIRECTORS' DUTIES & LIABILITIES



Textbook Chapters 11, 12 & 13

# Topic 6 - Learning Objectives



Directors' duties at common law and statute



Directors' liabilities



Relief from breach of duties



Reading: Textbook Chapters 11-13

*Refer also to Topic 6 – Directors' Duties and Liabilities Summary in OneDrive*

# Directors' Duties 1

Chapter 11



# Chapter 11 - Directors' Duties



Overview of duties



The duty of care



The duty not to engage in wrongful/reckless trading



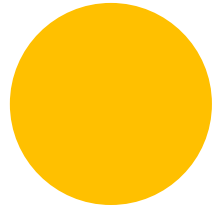
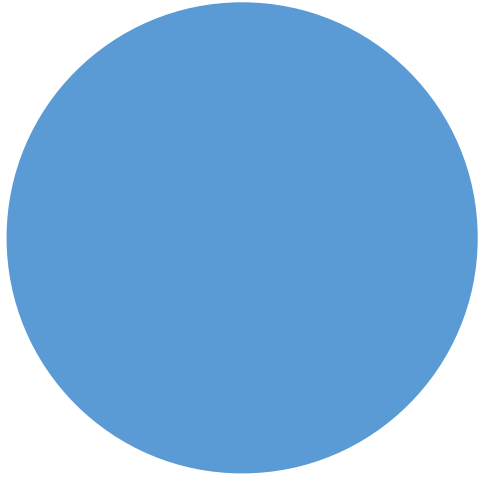
The duty to act in good faith in the best interest of the company



Duty to retain discretion



The duty to act for a proper purpose



# Overview of Duties

# Directors' Duties (table form, also refer to summary document)

DUTIES	Common/General Law	Statute
Care, skill and diligence	<ul style="list-style-type: none"> <li>Duty to act with reasonable care and diligence – this includes skills</li> </ul>	<ul style="list-style-type: none"> <li>S157(1) CA – act honestly and use reasonable diligence</li> <li>Administrative duties – general disclosure, keep accounting records, AGM, annual returns</li> <li>Liability for wrongful trading – s239 IRDA</li> </ul>
Loyalty and good faith	<ul style="list-style-type: none"> <li>Duty to act in good faith in the interest of the company</li> </ul>	<ul style="list-style-type: none"> <li>S157(1) CA – act honestly and use reasonable diligence</li> <li>Liability for fraudulent trading – s238 IRDA</li> </ul>
	<ul style="list-style-type: none"> <li>Duty to retain discretion</li> </ul>	
	<ul style="list-style-type: none"> <li>Duty to use proper purpose</li> </ul>	
	<ul style="list-style-type: none"> <li>Duty to avoid conflict of interests</li> </ul>	<ul style="list-style-type: none"> <li>S156 CA – disclosure</li> <li>S157(2) – improper use of info and position</li> <li>S162 – financial assistance to director</li> <li>S163 – financial assistance to director related companies</li> <li>S168, 169 &amp; 172 – directors' remunerations and benefits</li> <li>Interested person transactions SGX Listing Manuel</li> </ul>

# Overview of duties

- Who owes the duties?
  - General law duties are owed by the following persons:
    - Directors
    - Senior executive officers / fiduciaries (a relationship of trust and confidence)
- Statutory duties:
  - Directors
  - Other company officers as defined in s 4 of Companies Act –  
““officer”, in relation to a corporation, includes —any director or secretary; a receiver and manager; and any liquidator”

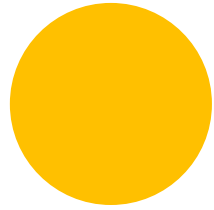
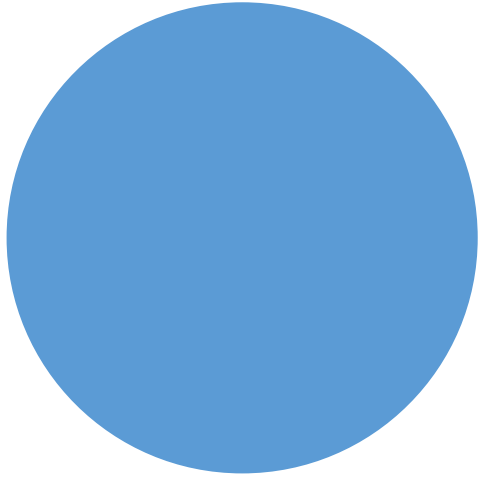
# Overview of duties

- To whom are the duties owed?
  - The company, so it is the company who can enforce breaches of duties.
  - In limited circumstances, an individual member — Bunninghausen v Glavanics (1999) 17 ACLC 1,247
- Who enforces the duties:
  - Depends on type of duty
    - Statutory duties, enforced by ACRA
    - General law duties, enforced by the company / liquidator



# Overview of duties

- What are the **consequences** of breaching a duty?
- **General law duties** – the company may sue the director for compensation or damages; or account of profits made
- **Statutory duties** – ACRA may enforce the penalties which include
  - To compel director to remedy the breach (administrative duties)
  - Criminal liabilities – the court may
    - Fine or imprisonment
    - Pay compensation to company
    - Disqualify from managing companies
    - Order compliance with statutes (s399 CA)



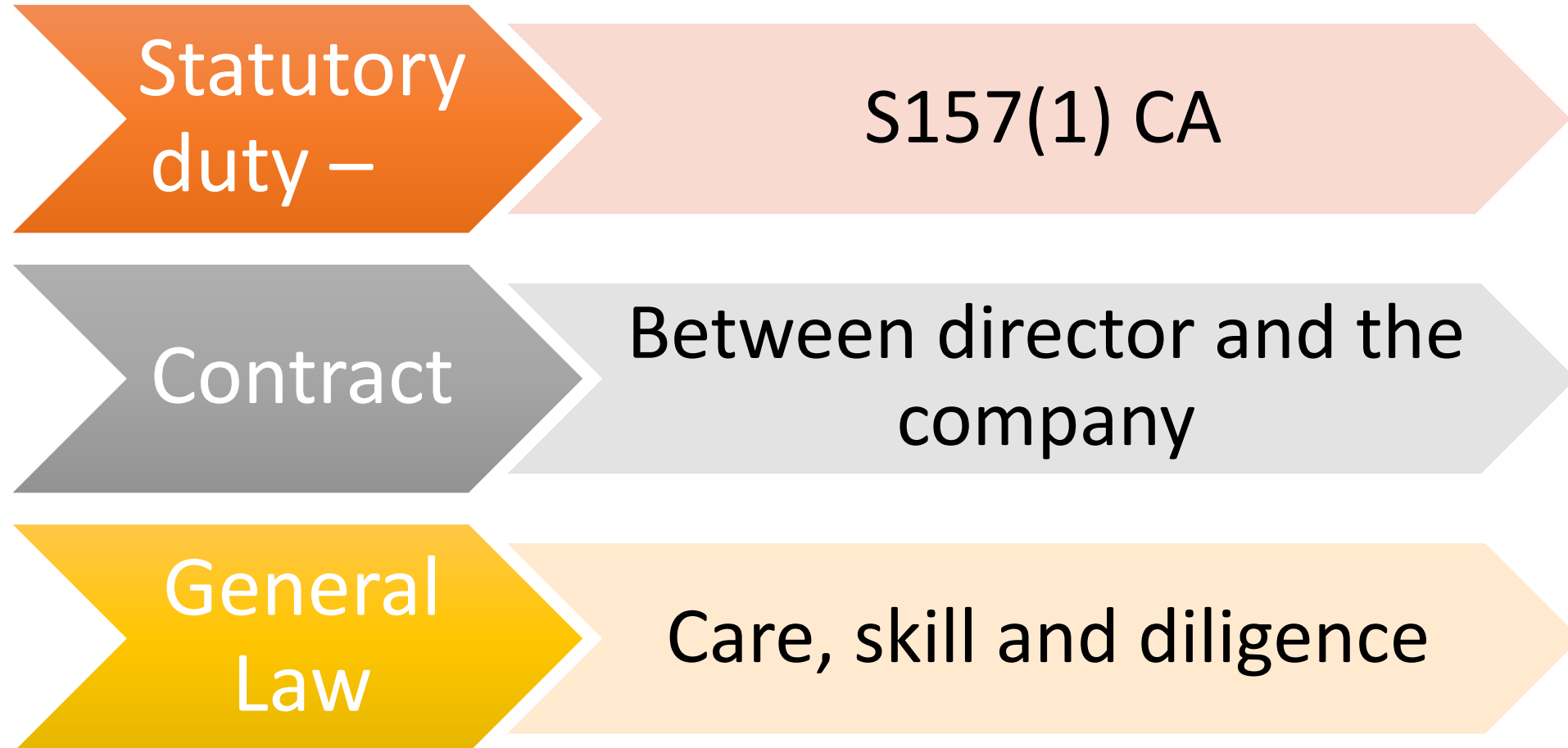
# The Duty of Care

# Section 157 Companies Act

S157 CA embodies the key aspects of directors' duties:

- (1) A director shall at all times act honestly and use reasonable diligence in the discharge of the duties of his office.
- (2) An officer or agent of a company shall not make improper use of his position as an officer or agent of the company or 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.

# The Duty of Care – Sources of duty of care



## Duty of care – **statutory duty** – s157(1) CA

- **157(1) CA** - A director shall at all times **act honestly** and **use reasonable diligence** in the discharge of the duties of his office.
- Use reasonable diligence includes care and skills.

# Duty of care - contract

- Often a duty of care arises from a contract between an executive director and their company.
- A term of the contract might be that the officer must exercise the care, skill and diligence expected of a person who occupies the position in question.

# Duty of care – general law/common law duty of care, skill and diligence

- *Re City Equitable Fire Insurance Co Ltd [1925]* – a director must exercise the same degree of skill and diligence which an ordinary man acting with reasonable care would as if he were acting on his own behalf, having regards to the circumstances of the case.

# Duty of care – the standards that are applied

- Same standard of care expected in common law and statutory law.
- What is the standard?
- *Daniels v AWA Ltd (1995)* – **minimum** standards of care, skill and diligence expected of all directors:
  - Basic understanding of the business and be familiar with the fundamentals
  - Under continual obligation to keep informed
  - Detailed inspection of day-to-day activities not required but need a general monitoring of company's affairs
  - Maintain familiarity with the financial status of the company by regular review of financial statements



# Duty of care – standards – reasonable care

- A director must exercise reasonable care.
- The standard of care is an **objective test**, whether the director has exhibited the same degree of care as a reasonable director found in his position.
- Lim Weng Kee v PP [2002] - standard is not fixed but depends on various factors such as the individual's role in the company, the type of decision being made, the size and the business of the company. The standard will not be lowered to accommodate any inadequacies in the individual's knowledge or experience (subjective test if the director claims to be an expert)
- Court will compare the director's conduct with that expected of a reasonably diligent person having both
  - a) The general knowledge, skill and experience that may be reasonably expected of a person carrying out the same functions and
  - b) The general knowledge, skill and experience which that director has - this increases the level of care and diligence rather decreases it

# Duty of care – standard - skill

- Skills depend on whether the director is executive or non-executive and whether he has special qualifications.
- Executive director – his conduct is tested against an objective body of expertise and knowledge possessed by people in the same type of position, ie, what would a **reasonably competent financial director** do in that circumstances?
- Non-executive director – no objective standard – too varied
- Special knowledge or experience – tested against the skill of a reasonable director with similar knowledge and experience.

# Duty of care – standard - diligence

- All directors are required to exercise the amount of diligence that would at least allow them to be familiar with the operations of the company's business and keep informed about the financial status of the company.
- Meetings – Singapore Code of Corporate Governance recommend disclosure of the number of meetings attended by directors, but they may still breach duty if they fail to exercise reasonable diligence in making decisions.


# Duty of care – delegation and reliance – defence – s157C CA

- Can a director delegate certain tasks to others and rely on those to perform the tasks properly?
- s157C CA allows a director to rely on reports, statements, financial data and other information as well as on professional or expert advice given by the following persons:
  - a) A reliable and competent employee
  - b) A professional adviser or expert
  - c) Any other director or committee member of directors

Provided that the director acts in good faith and had made proper enquiry and had no knowledge that such reliance was unwarranted.

# Duty of care – does the court interfere with business decisions?

- The court generally do not interfere with bad business decisions made in good faith, as long as the directors made the decisions in the honest and reasonable belief that they were for the best interests of the company, even if those decisions turned out subsequently to be money-losing ones.
- This is also known as “**business judgment rule**”
- Intraco Ltd v Multi-Pak Singapore Pte Ltd [1995] 1 SLR 313 – directors made a bad commercial decision, but they did not make a negligent decision, thus not liable for the loss.
- Vita Health Laboratories Pte Ltd v Pang Seng Meng [2004] – director ordered excessive perishable stock based on sales forecasts – held not liable for the losses resulting from his actions.



The Duty not to Engage in  
Fraudulent or wrongful trading  
(New)

# The duty not to engage in wrongful/fraudulent trading -

- Creditors have no means to know the true financial affairs of the company, some directors still carry-on trade when the company is insolvent.
- **Section 239 Insolvency, Restructuring and Dissolution Act (IRDA 2018)** deals with **wrongful trading** - a company is deemed to trade wrongfully if it incurs debt or liabilities when insolvent (or becomes insolvent as a result of incurring such debt or liability), without reasonable prospect of meeting them in full. A director who permits a company to engage in wrongful trading can be personally liable.
- Criminal penalty for wrongful trading – s239(6) IRDA - shall be guilty of an offence and shall be liable on conviction to a fine not exceeding \$10,000 or to imprisonment for a term not exceeding 3 years or to both.
- **Section 238 IRDA** deals with **fraudulent trading** – if during judicial management or winding up, it appears that the company has been carried on business with intent to defraud creditors of the company for fraudulent purpose, the court may make the person (director) who was knowingly a part to the carrying on of the business personally liable for all or any of the debts or other liabilities of the company.
- Criminal penalty for fraudulent trading – s238(4) - every person who was knowingly a party to the carrying on of the business with that intent or purpose shall be guilty of an offence and shall be liable on conviction to a fine not exceeding \$15,000 or to imprisonment for a term not exceeding 7 years or to both.



Duty to Act in Good Faith in the  
Best Interest of the Company



# The duty to act in **good faith in the best interests** of the company

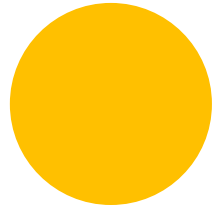
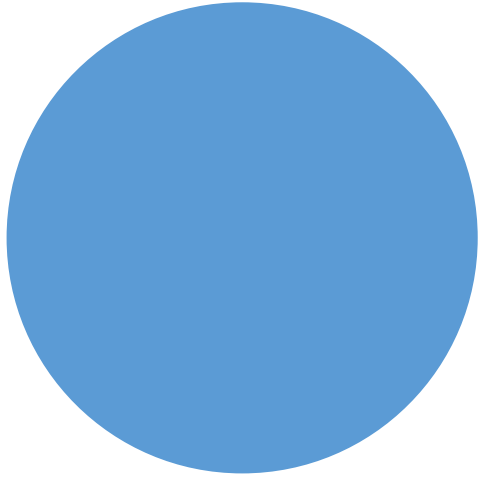
- What is meant by good faith (bona fide) - Townsing Henry George v Jenton Overseas Investment Pte Ltd ) creditors' voluntary liquidation) [2007] 2 SLR 597 – “to act honestly in the discharge of his duties as a director”.
- See also s157(1) CA - A director shall at all times **act honestly** and **use reasonable diligence** in the discharge of the duties of his office.
- What are the company's interests?
  - Interests of members
  - Company
  - Creditors
  - Other companies within the group of companies
  - Employees, customers, suppliers and the community

# The duty to act in good faith in the best interest of the company

- The company separate from its members
  - Question as to whether there is a duty to act in the interests of the company as a separate entity independent from its members - general view is that directors owe the duty to the company first
- Members
  - The interest of the company are generally those of its members, sec 159 CA – directors must take account of the interests of the company as a whole – balance between majority and minority
- Creditors
  - Where the company is insolvent, the interests of the company becomes those of the creditors rather than its shareholders
  - ss238 & 239 IRDA

# The duty to act in good faith in the best interest of the company

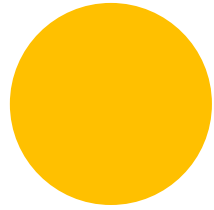
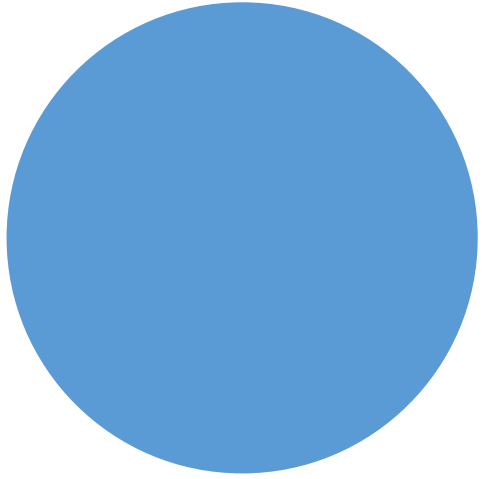
- Corporate groups:
  - Each company is to be treated as having own interest even if the company is wholly-owned subsidiary
  - Director of subsidiary must act in the interest of the subsidiary and not the parent company or any other company
- Employees, customers, suppliers and community:
  - Company law requires that as a general rule, the interest of employees and other stakeholders should not be given priority over the interests of members
  - S159(a) CA



# Duty to Retain Discretions

# The duty to retain discretions

- What does it mean to retain discretions (freedom to decide)?
  - Directors must retain the freedom they have to make decisions on behalf of the company
  - The directors cannot undertake or agree that they will not exercise powers given to them in the constitution or under the *Companies Act*
  - For example, issue of new shares are given to members to decide in general meeting, but decision to issue new shares are for the directors to decide. They must do this in the best interest of the company, not in the best interest of a majority shareholder who fears dilution of voting power.



Duty to Act for a  
Proper Purpose

# The duty to act for a proper purpose

- What are proper purposes?
  - Depends on the constitution
  - Section 157A CA – directors may exercise all powers of the company except any powers that the *Companies Act* or the company's constitution requires the company to exercise in a general meeting of members.
- How do courts determine whether director has acted for the proper purposes?
  - Two step analysis:
    - Determine the legal purposes for which the power in question has been given
    - Examine facts of the case, the intentions of the director and the actual purpose for which the director exercise the power

# The duty to act for a proper purpose - examples

- The power to issue shares
- The most common proper purpose is to raise capital; however, can also issue shares to:
  - Provide employee with financial incentive via employee share plan;
  - Enter joint venture with another company
- Improper purposes include the purpose of
  - Diluting the shareholding of a member;
  - Entrenching control of the company in certain shareholders
  - Attempting to reduce to a minority position, a member who holds a majority of the voting power
  - Directors maintaining control of the company.
- *Howard Smith v Ampol Petroleum Ltd (1974)*



# Tutorial Questions on doc