

# **A Study of Cases against Directors in Singapore**

**(Based on historical data)**

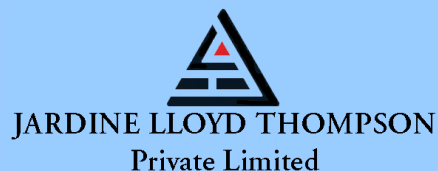
Conducted by:

**Corporate Governance and Financial Reporting Centre  
NUS Business School, National University of Singapore**

Commissioned by:

**Jardine Lloyd Thompson Private Limited**

**April 2004**



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JARDINE LLOYD THOMPSON  
Private Limited

## About Jardine Lloyd Thompson Private Limited

Jardine Lloyd Thompson (JLT) Private Limited began its operation in 1969, and has since gained a steadfast reputation as one of Singapore's top retail insurance brokers. They are part of the Jardine Lloyd Thompson Group, the world's fifth largest international insurance broker and the largest UK and European based broker quoted on the London Stock Exchange. The JLT Group operates in 30 countries, employs over 4,000 staff and services premiums of approximately £3 billion.

JLT has clearly made the connection between D&O Insurance and Corporate Governance. We participate in corporate governance associations and work with related bodies in an effort to stay at the forefront of this important area. Effective transfer of director risk is essential for sound functioning of a Board and also for a company to attract the best independent/non-executive directors.

JLT's local team of more than 60 insurance professionals is highly qualified and experienced in handling all lines of insurance within specific industry segments. Their aim is to provide strategic and comprehensive risk solutions that help clients compete more effectively and improve their financial performance. When client's needs dictate, JLT is able to push beyond the traditional boundaries of insurance and produce highly innovative and advanced structures that integrate alternative risk transfer and other insurance related techniques.

As a leading broker, JLT hires the best talents who consistently deliver industry leading solutions and services of an exceptional level. These are the qualities that set JLT apart from other brokers and earned them the Asia Insurance Industry 'Broker of the Year' award for the past three consecutive years from 2001-2003.

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# CONTENTS

<b>Executive Summary.....</b>	<b>5</b>
<b>Objective.....</b>	<b>7</b>
<b>Methodology.....</b>	<b>7</b>
<b>Number of Cases.....</b>	<b>7</b>
<b>Party Initiating Action.....</b>	<b>8</b>
<b>Nature of Litigation.....</b>	<b>10</b>
<b>Judgments.....</b>	<b>13</b>
<b>Number of Directors Involved.....</b>	<b>15</b>
<b>Industry Associated with the Cases.....</b>	<b>15</b>
<b>Conclusion.....</b>	<b>16</b>

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## Executive Summary

This “Study of Cases against Directors in Singapore” was conducted by the Corporate Governance and Financial Reporting Centre, a unit of NUS Business School, National University of Singapore and commissioned by Jardine Lloyd Thompson Private Limited, Singapore with the objective of understanding the pattern of directors’ and officers’ liability litigation in Singapore. The study is based on the historical legal records obtained from legal databases and does not cover cases filed outside Singapore.

Some major findings that may be derived from the study are:

1. The number of litigation cases against directors is on the rise in Singapore.
2. More cases were initiated against directors of private limited companies as compared to directors in public limited companies.
3. The probability of a director winning a suit is very low. Based on historical trends, the party initiating the suits in the study won in 71% of the cases.
4. The claimant might often bring an action under many sub-heads so as to increase his chance of winning though it may not be easy to prove that a director has breached his duty of good faith or duty of care to the company.
5. The directors in the construction industry appear to be attracting more legal suits against them as compared to those from the other sectors.

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## Objective

The study examines the cases brought against company directors in Singapore in the period 1975 to 2003 for the purpose of understanding the pattern of directors' and officers' (D&O) liability litigation in the country.

## Methodology

The study was conducted by the Corporate Governance and Financial Reporting Centre (CGFRC), a unit of the NUS Business School, National University of Singapore and commissioned by Jardine Lloyd Thompson Private Limited (JLT), a leading provider of insurance and risk management expertise in the Asian region. The data for the study was obtained from historical legal records through legal databases for the period 1975 to 2003. The study did not cover the cases filed outside Singapore against directors of Singapore companies.

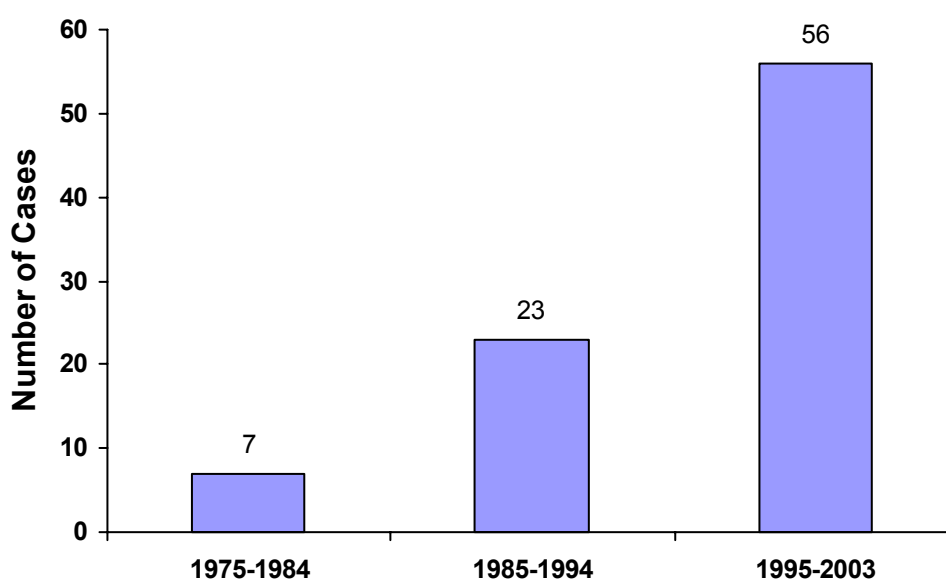
## Number of Cases

The study found 86 cases recorded in Singapore against directors between 1975 and 2003. Of these, 79 cases involved private limited companies while only seven cases involved a public limited company. This may be due to two reasons. First, for the shareholders in a public company, many may prefer to sell away their shares in the stock market, i.e. 'walk out' of the company if they are unhappy with the way the management has been dealing with the company, rather than taking a suit against the directors for breach of duty. A legal action will most likely affect the share price adversely, making it harder for the shareholders to sell away the shares in future. Further, in Singapore, a derivative or representative action, i.e. shareholders taking an action in the name of the company to seek redress on injury caused to the company, is still limited to unlisted companies under Section 216A of the Companies Act, Cap 50. For an action alleging oppression or injustice caused to the shareholder himself/herself or a group of shareholders in their capacity as shareholders (as what the Americans call "class action") pursued under Section 216 of the Companies Act, the applicant(s) will have to bear his (their) own cost and is unable to apply for indemnification by the company. Therefore, it is very unlikely that a shareholder of a public company in Singapore will pursue a legal action against an errant director in court. Second, the standard of corporate governance is arguably higher in a public company than in a private company due to the legal requirements (e.g. independent directors, timely reporting and disclosure etc.) and the organisational structure (e.g. more professional staff running the company). This

standard has certainly increased over the years as can be seen from the fact that out of the seven cases concerning public companies, four cases happened before 1985.

The number of cases (see *figure 1*) has been steadily rising over the last three decades probably due to increased awareness about corporate governance issues and directors' duties. The increasing voice of minority shareholders, either individually or through their associations, is likely to lead to more such cases in Singapore.

**Figure 1: Number of Cases**



## Party Initiating Action

*Figure 2* shows the percentage of cases initiated by different parties. Creditors initiated the most number of cases (excluding criminal actions) against directors, accounting for just over a fifth (21%) of all the cases. These cases generally involved bank creditors suing directors for personal liability incurred as a result of them guaranteeing loans made by the banks to the companies in which they were directors.

The company itself initiated the second highest number of cases accounting for 19% of all the cases. These cases included claims made by the liquidators on behalf of the companies in winding up situations. Most of these actions involved claims against former directors for breach of directors' fiduciary duties owed to the companies. These usually took place after the company had been bought over by a new owner or when the board

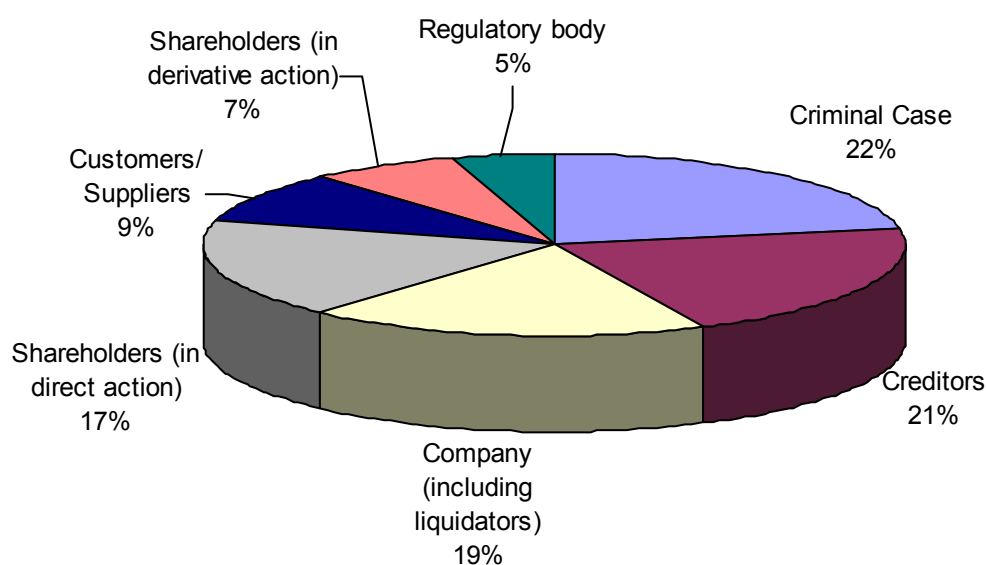
(commonly through the majority shareholders or their nominees) decided to take action against one or more errant directors.

Shareholders making direct claims (mainly for oppression under Section 216 of the Companies Act) accounted for 17% of the cases brought against directors. There were only five cases where the shareholders made or applied to make derivative claims on behalf of the company either under common law derivative actions or under Section 216A of the Companies Act.

9% of the cases were initiated by customers who sued the companies and the directors trying to make them personally liable for torts<sup>1</sup> committed by their companies. There were also four cases, where the Attorney-General objected to the former directors' applications to take part in the management of companies as these directors had been disqualified from being directors for offences they had committed under the Companies Act.

The Public Prosecutor initiated 22% of the cases against the directors in various company-related criminal actions such as criminal breach of trust, fraudulent trading, corruption etc.

**Figure 2: Party Initiating Action**



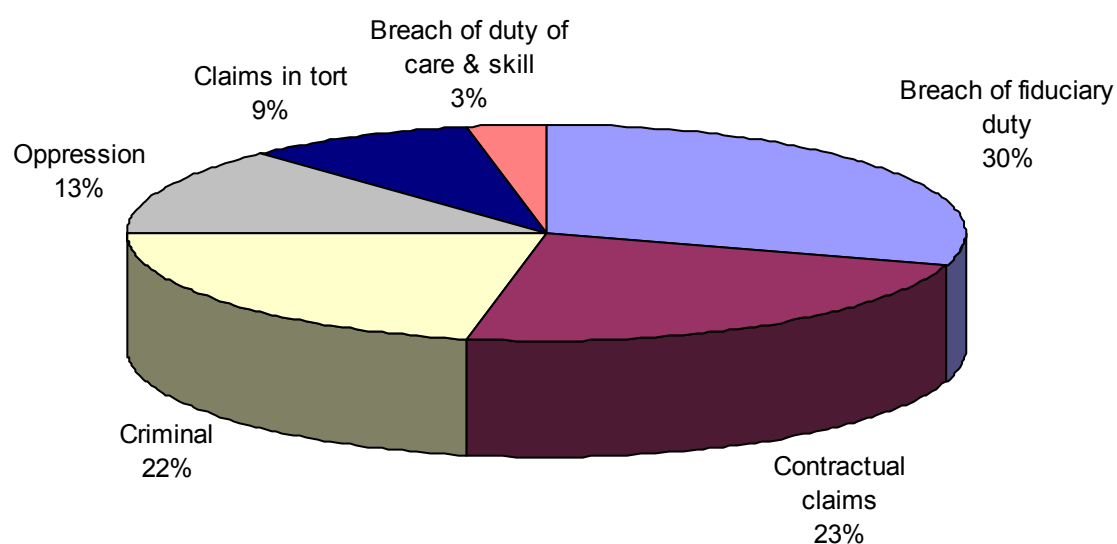
<sup>1</sup> Torts - Damage, injury, or a wrongful act done willfully, negligently, or in circumstances involving strict liability, but not involving breach of contract, for which a civil suit can be brought. (source: [www.dictionary.com](http://www.dictionary.com))

## Nature of Litigation

In 78% of the cases (see *figure 3*), civil suits were taken against the directors and a large proportion of these cases concerned breach of duties to the company, including fiduciary duties (30% of total number of cases) and duty of care (3%). Of the directors accused of breach of fiduciary duties, many (36%) had more than one reason cited against them (see *figure 4*). For instance, in *Low Hua Kin v Kumagai--Zenecon Construction Pte Ltd (In Liquidation)* [2000] 3 SLR 529, the director of the company, Low Hua Kin, caused the company, to borrow from a bank in order to purchase enough shares in listed companies so that he could be appointed director in the latter. He also unilaterally changed the name and memorandum of the company without informing the minority shareholder. Therefore, in a liquidation proceeding to wind up the company, he was alleged to have not acted in the bona fide<sup>2</sup> interest of the company, abused his power as a director, put himself in a situation of conflict by misusing corporate assets and also acted oppressively towards the minority shareholder.

Conflict of interest appears to be the most frequently cited single reason (see *figure 4*) for claims of breach of fiduciary duties (40%).

**Figure 3: Nature of Litigation**



<sup>2</sup> Bona fide - made or carried out in good faith; sincere (source: [www.dictionary.com](http://www.dictionary.com))

**Figure 4: Fiduciary Duties**

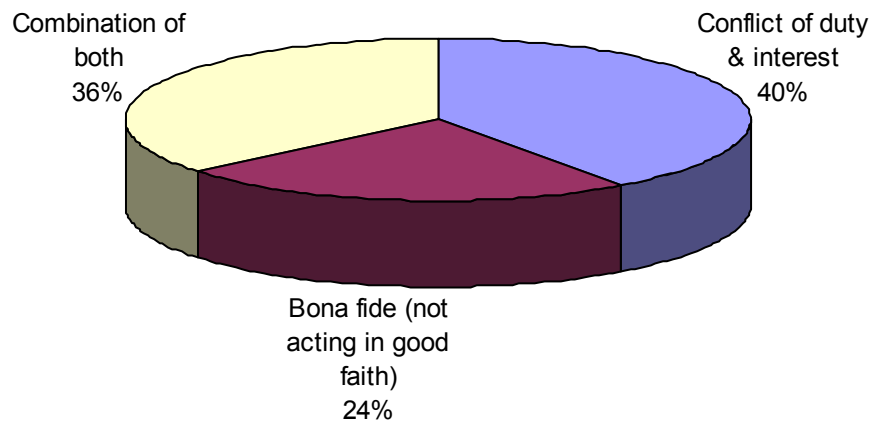
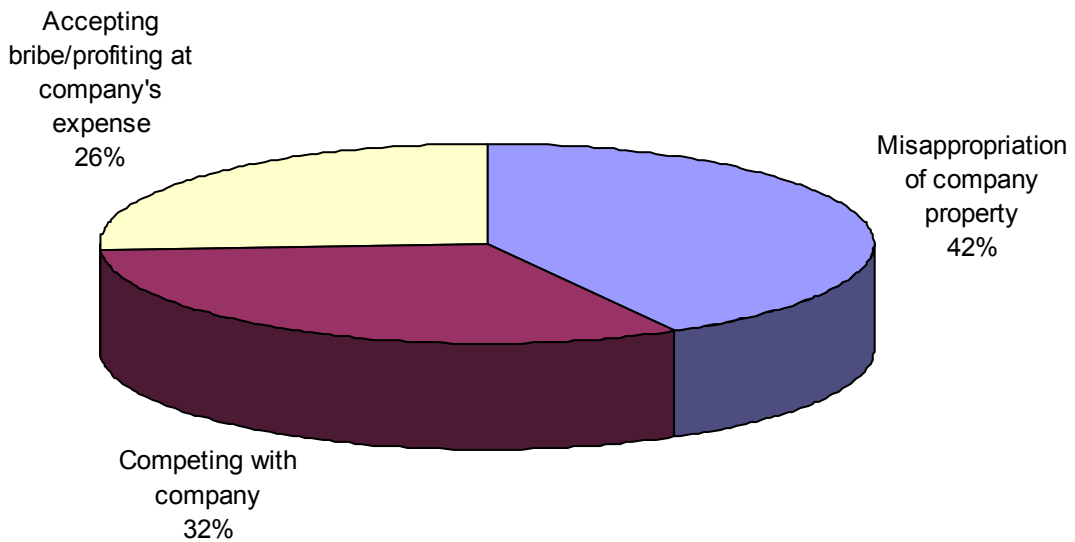


Figure 5 shows the nature of conflict of interest which the directors were accused of. Of the 19 cases involving conflict of interest, 42% were accused to have misappropriated the company's property, 32% for competing with the company and 26% for accepting bribes or profiting at the company's expense.

**Figure 5: Nature of Conflict**



The reason that most of the cases involving breach of fiduciary duty fall under conflict of interest may be due to the fact that it is easier to prove conflict of interest, as compared to more fuzzy concepts such as lack of good faith (bona fide) and proper purpose. In

fact, out of the six cases studied concerning a claim in bona fide, the claimants only managed to win two of the cases. As mentioned by a judge in one of the cases, matters of management should be left to the board of directors and the correctness of such decisions, if made in good faith, would not be questioned by the court (per Goh Joon Seng J, in *Re Winpac Paper Products Pte Ltd; Seow Tiong Siew v Kwok Low Mong Lawrence & Ors* [2000] 4 SLR 768) and it is not always easy to prove mala fide<sup>3</sup>. For instance, in *Re Winpac Paper Products Pte Ltd* case, the court held that mere refusal to initiate legal action against a third party was not sufficient to show that the board has not acted in the bona fide interest of the company, because it might be due to good commercial reasons.

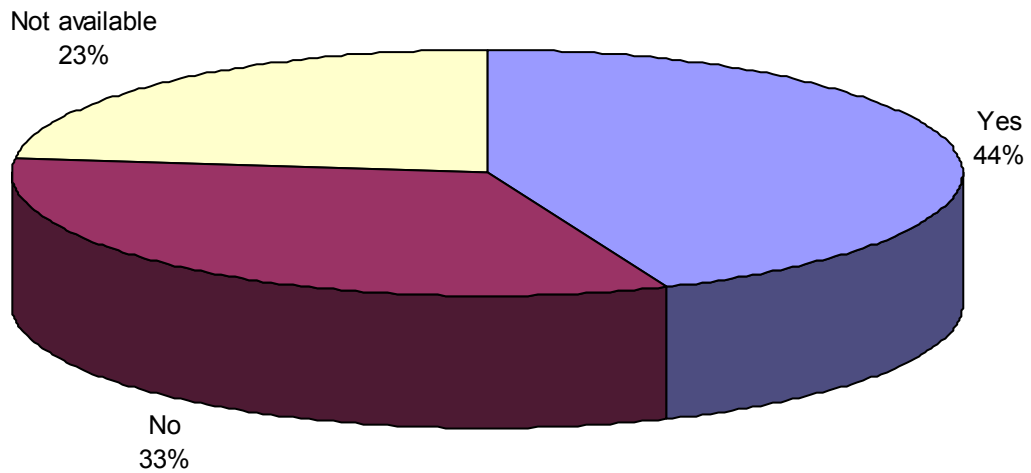
Similarly, it is not easy to prove that the director has breached his duty of care, skill and/or diligence. Of the three cases involving breach of duty and care, skill and/or diligence, two involved a breach of duty of care and one a breach of duty of skill/diligence. The three cases that fall under this head may throw some light as to how and when a director will be considered as liable for breach of his duty of care, skill and/or diligence. In *Re Kie Hong Shipping (1971) Pte Ltd* [1984 -- 1985] 1 SLR 544, an executive director who was “totally powerless” against the majority shareholder, who was also his uncle, and not recovering the debts owed to the company by some affiliated companies controlled by the majority shareholder, was considered “greatly negligent in the management of the affairs of the company”. Similarly, in *Swee Leong Cheng v Project Aqua Culture & Trading Co Pte Ltd* [1988] 1 SLR 557, a regular military officer who had no prior knowledge of business found that he could not plead ignorance when he was charged with failing to file annual returns with the Registrar of Companies. However, when a board made an honest business decision, it could not be accused to have breached its duty of diligence to the company merely because the decision turned out to be a bad one on hindsight (*Intraco Ltd v Multi--Pak Singapore Pte Ltd* [1995] 1 SLR 313).

The directors were alleged to have benefited at the company's expense in 44% of all the cases filed against them (*see figure 6*), while no data was available in 23% of the cases. In all these 44% cases the gain for the directors was alleged to have been monetary in nature.

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<sup>3</sup> Mala fide – with or in bad faith (Source: [www.dictionary.com](http://www.dictionary.com))

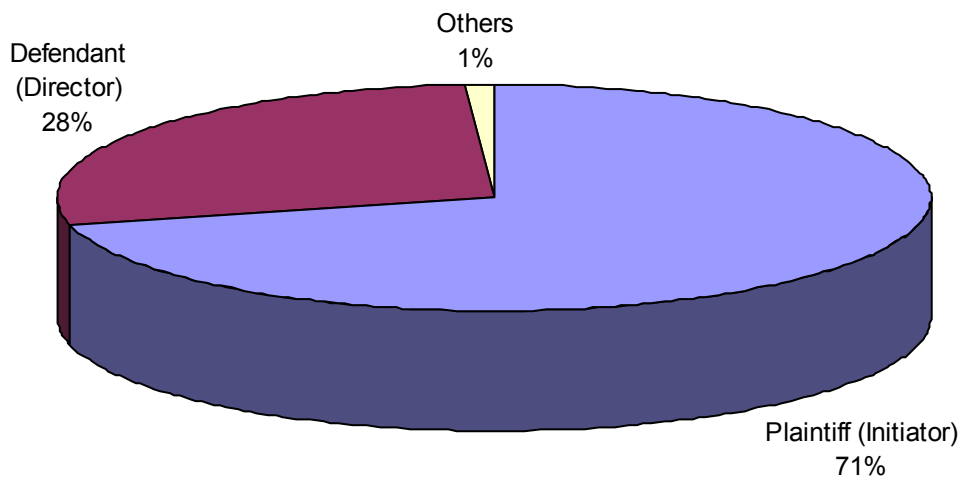
**Figure 6: Did the Directors Benefit?**



## Judgments

As shown in *figure 7*, the directors won in just over a quarter of the cases (28%) through successful defence while the party who had initiated action won in just under three-quarters (71%) of the cases. This indicates that actions against directors are often successful. The single case listed as “Others” in *figure 7* involved two directors being charged, with one acquitted and the other sentenced to four years imprisonment.

**Figure 7: Who Won the Case**

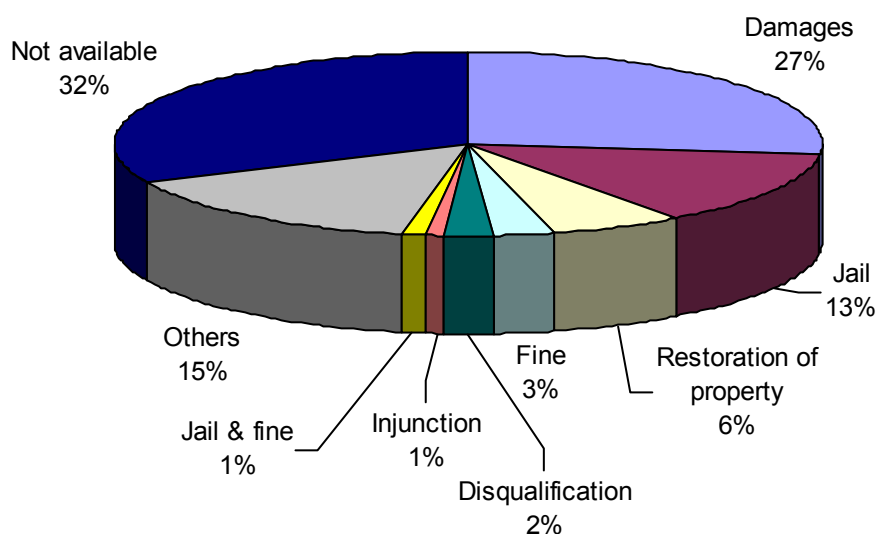


As shown in *figure 8*, damages were awarded to the plaintiff in nearly a third of the cases (27%). In the cases where the exact amount of damage awarded was mentioned, the amount ranged from S\$80,000 to S\$53.3 million.

Restoration of property was ordered in 6% of the cases and directors were disqualified in 2% of the cases while other remedies, such as allowing the plaintiff to proceed with the action in the name of the company, ordering a retrial of the case, granting a winding up petition, ordering the defendant to purchase plaintiffs' shares etc. occurred in 15% of the cases.

For the criminal cases, the directors who were convicted mostly received jail sentences ranging from 3 months to 8 years. However, the trend may change when the proposal by the Company Legislation and Regulatory Framework Committee (CLRFC) is implemented. In paragraph 4.6 of the CLRFC Report, the Committee recommended a total review of the Companies Act with the objective of decriminalizing those provisions where civil and regulatory sanctions would be sufficient. The example cited by the CLRFC was abolishing of criminal sanctions for directors who fail to acquire the requisite shareholding qualification (Section 147(4) Companies Act). Nevertheless, it remains to be seen as to how far the law will be relaxed in cases of more serious corporate misbehaviour such as fraudulent trading. In addition, other than the provisions in the Companies Act, a director or officer also runs the risk of breaching relevant laws such as the Penal Code (e.g. criminal breach of trust) and the Securities and Futures Act (e.g. insider trading).

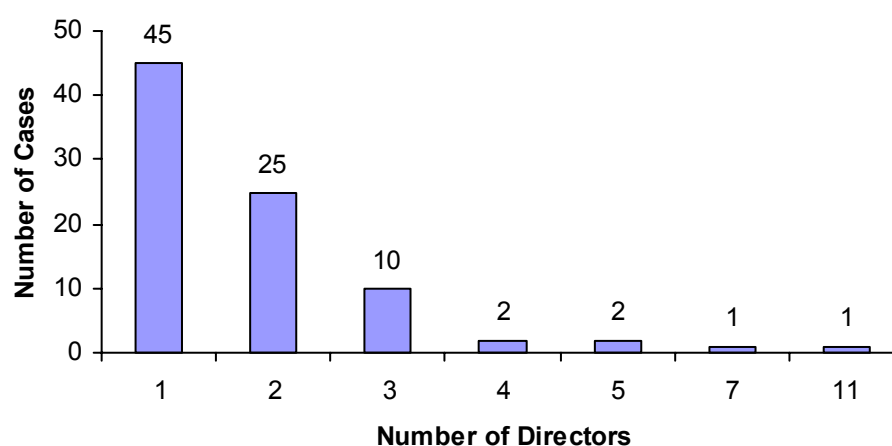
**Figure 8: Nature of Remedies**



## Number of Directors Involved

In almost half the cases (52%), a single director was involved as the defendant (see *figure 9*) while another quarter of the cases involved two directors. 10 cases (12%) had three directors as the defendants while another six cases (7%) had four or more directors against whom the cases were initiated. This can be attributed to the fact that since a majority of the companies involved were private companies, the boards tended to be small. However, it was also found that in most of the cases involving more than one director as the defendant, the initiators would usually be parties other than the companies themselves. A possible reason is that as the ability to sue, being part of the board's general management power, lies in the hand of the board, it is very unlikely that the board will choose to sue a majority of its brethren. This can be supported by the fact that in the very few company-initiated suits against more than one director, the plaintiffs were the liquidators/official receivers or the minority shareholders who were able to initiate derivative suits against the directors with the leave of the court.

**Figure 9: Number of Directors Involved**



## Industry Associated with the Cases

It is interesting to note that the real estate and construction industry accounted for nearly one quarter of the cases while 15% of the cases were in the industrial goods and services sector and another 13% in the transportation sector. One reason for the high incidence of cases in the construction sector may be because the recent economic downturn has hit the real estate and property sector especially hard and with more

construction companies being wound up or sold, more instances of corporate misbehaviour have been uncovered by the liquidators or the new owners.

A complete breakdown of the industry sector associated with the cases is shown in *Table 1*.

**Table 1: Industry Associated with the Cases**

<b>Industry</b>	<b>% of Cases</b>
Accounting	1%
Agriculture	2%
Automotive	2%
Computers & Software	3%
Energy & Environment	2%
Financial Services/Banking	6%
Food & Beverage	5%
Human Resources	2%
Industrial Goods & Services	15%
Management	2%
Media & Entertainment	5%
Pharmaceuticals & Biotechnology	1%
Real Estate & Construction	24%
Retail & Consumer Services	5%
Transportation & Logistics	13%
Others	12%

## **Conclusion**

This study is probably the first of its kind to be conducted in Singapore. More research is needed to conclusively prove some of the issues raised in this report. However, some preliminary comments may be made based on the findings from this study. First, the number of litigation cases against directors is on the rise in Singapore judging from the upward trend over the years. Although this may be partly due to an increase in the number of companies over time, we believe that the likelihood of litigation increased over time. Second, based on historical trends, if a director is sued the probability of him winning the suit is less than 30%. Third, although it may not be easy to prove that a director has breached his duty of good faith or duty of care to the company, the claimant will often bring an action under many sub-heads so as to increase his chance of winning. This is usually not difficult especially when the director has made some personal gains from the transactions in question. Fourth, directors in the construction industry appear to

be attracting more lawsuits as compared to those from other sectors. Although the economic downturn in the sector might have played a part, the standard of corporate governance in the industry should be more closely looked at in the future to see how it may be improved.

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## About Corporate Governance and Financial Reporting Centre

The Corporate Governance and Financial Reporting Centre is a unit of NUS Business School, National University of Singapore. The Centre's mission is to research, disseminate and promote best practices in corporate governance and financial reporting. It is one of the few centres in the world for the promotion and development of good corporate governance and better financial reporting.

A hallmark of the Centre is the strong industry orientation in its activities and projects. The current and proposed portfolio of activities of the Centre includes topics such as boardroom practices, executive compensation, creative accounting, quarterly reporting and investor relations. It encourages a convergence of academics and practitioners around some of the key challenges of corporate governance and financial reporting in organizations. Being research-led and industry-oriented, the centre is at the cutting edge of theory and practice and it helps to bridge the gap between leading academic work and the needs of practitioners.

The centre collaborates with reputed organisations like Standard and Poor's, Singapore Institute of Directors (SID), Securities Investors Association Singapore (SIAS), Institute of Certified Public Accountants of Singapore (ICPAS), Federal Insurance Company, Singapore (Chubb Insurance) and Jardine Lloyd Thompson Private Limited on various projects that seek to increase awareness on corporate governance issues. We welcome requests for collaboration from organisations within and outside Singapore to undertake projects that will further the cause of good corporate governance.

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