



INSIGHTS

by ML CHAMBERS

Shareholder Decisions – The Power of the Vote

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About

When can shareholders make management decisions in connection to the company? Can shareholders overrule their board's business decisions? What decisions (if any) must be reserved to the shareholders?

In this brief note, our directors explore some of these questions.

SHAREHOLDER PARTICIPATION

Shareholders who hold ordinary shares generally have the right to attend and vote at any general meeting. It is also significant to point out that a mere equitable or beneficial interest in shares would ordinarily not entitle one to such voting rights.

General meetings are meetings convened for shareholders and the two most common illustrations of the same are annual general meetings (or AGMs) that a company must convene after the end of each financial year and extraordinary general meetings that can be requisitioned by shareholders holding not less than 10% of the total number of paid-up shares or by directors of the company (if permitted under the company's constitution).

Unlike shareholders, a "director may at any time summon a meeting of the directors".

That said, where listed companies are concerned, the MAS Code of Corporate Governance 2018 does prescribe that "[t]he company communicates regularly with its shareholders and facilitates the participation of shareholders during general meetings and other dialogues to allow shareholders to communicate their views on various matters affecting the company."

DEFAULT POSITION

Prior to 1897, a company was regarded as an association of its shareholders (whom collectively represented the will of the company at a general meeting) and directors were deemed as "agents" of the company's shareholders.

With the introduction of the separate legal entity doctrine (where a company is a separate legal entity from its shareholders), it is now clear that directors owe their duties to the company and not to individual shareholders. Whilst shareholders "own" the company, the directors "manage" and run the company's day-to-day to operations.

This has given rise to the division of powers between directors and shareholders which, in Singapore, has now been given effect in 2003 through statute (section 157A of the Companies Act (Cap. 50); "Powers of directors").

Section 157A of the Companies Act (Cap. 50); “Powers of directors”

157A.—(1) *The business of a company shall be managed by or under the direction of the directors.*

(2) *The directors may exercise all the powers of a company except any power that this Act or the memorandum and articles of the company require the company to exercise in general meeting.*

[emphasis added in italics and bold italics]

Where section 157A is qualified by the words “*except any power that this Act*”; this includes decisions to amend the constitution of the company, alteration of share capital, issuance of shares, reduction of share capital, disposal of the whole or substantially the whole of the company’s undertaking or property, etc, which have to be passed at a general meeting of shareholders. Though, these are the exceptions to the norm.

The general position, remains, that shareholders cannot ordinarily interfere with the board’s exercise of its management powers.

That said, shareholders (with enough vote count) are technically able to remove or appoint directors to a board, amend the company’s constitution, etc, which may indirectly achieve significant control over the board.

EXPRESS CONTRACTUAL AGREEMENT

The Singapore Court of Appeal (affirming a High Court decision), however, has made clear that section 157A of the Companies Act (Cap. 50) merely establishes a “default rule” which can be varied by the company’s constitution.

What this therefore means, is that shareholders ought to treat the company’s constitution (and the drafting of its terms) with great care. For instance, model / template constitutions adopted by companies often include an article which expressly echoes section 157A:-

Powers and duties of directors

77.—(1) The business of a company is managed by or under the direction or supervision of the directors.

(2) The directors may exercise all the powers of a company except any power that the Act or this Constitution requires the company to exercise in general meeting.

If unamended, section 157A and article 77, would be read as shareholders accepting “the [general] compact between the shareholders and the directors ... that while the former own the company, the latter manage it.”

Ultimately, in Singapore, the division of powers between the board of directors and the shareholders is a “matter of contract”. Shareholders therefore should do well to note that any wish for a larger management-say should be negotiated at the outset (with carefully a considered company constitution and shareholders agreement) and, if done, can potentially prevent the need for costly protracted litigation.

That said, shareholders should also carefully weigh whether it makes (or not) for sound corporate governance practice to carve out substantial scopes of management decisions from the board.

After all, the default position is founded on good reasons; i.e. – “... directors are fiduciaries of the company whereas shareholders are not. Directors are therefore required, always, to act in the best interests of the company. Shareholders are not fiduciaries of the company – shareholders are entitled to vote in their own personal interests on any shareholders’ resolution. This is so even if their personal interests conflict with the company’s best interests.”

IMPLIED SHAREHOLDER RESERVE POWERS

Where shareholders did not at the outset contract for themselves specific management rights, there may still be room for the court to nonetheless “imply” a term that to place a particular management power in the shareholders.

Such implied reserve powers will only be permitted to be invoked in limited circumstances (and only as a matter of “necessity”) where there is either (a) a deadlock; or (b) the deadlock cannot be broken by the appointment of additional directors and/or the removal of existing directors in a general meeting. There must also be sufficient shareholder votes to pass such relevant resolutions (if not, implying any reserve power would have no practical purpose).

Whilst the courts have made clear that a shareholders’ ability to commence a section 216A (derivative action) would not per se prevent the court from implying reserve powers, the shareholders’ ability to do so will nonetheless factor into the aforesaid “necessity” analysis with every case taken and assessed on its own facts.

KEY TAKE-AWAYS

- The default position is that the power to manage a company is vested with its board. Shareholders can, however, contract (vide the company’s constitution) to recalibrate the division of powers between the board of directors and the shareholders.
- The company’s constitution is of paramount importance and shareholders should devote sufficient intellectual capital to its drafting and to delineating the boundaries of shareholder and director powers at the outset.
- Whilst the courts have made clear that they are nonetheless able to imply reserve management powers for shareholders, shareholders must note that the criteria for such implication have been framed so stringently that one author has termed such potential scenarios as “black swan events”.

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Mark Lee Chambers Law Corporation is a boutique litigation and arbitration firm specialized in high stakes complex litigation with a particular focus in corporate law, joint ventures, shareholder and boardroom related matters.

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