



INSIGHTS

by ML CHAMBERS

A Director's Perspective: Exposure, Risks and Personal Liability

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About

In this article, we explore the trite concept of limited liability of companies juxtaposed against the “ironic” onerous personal liability / exposure that directors face in the course of their management and running of that limited liability entity.

Whilst not intended to be exhaustive, this article attempts to take the reader through the multitude of scenarios where a director may find herself / himself staring down the “barrel” of a lawsuit / regulatory enforcement action and risking personal liability.

The Incorporation Reality – Balance of Power

Section 19(5) of the Singapore Companies Act 1967 (“CA”) underscores a fundamental tenet of company law – i.e. once a company is incorporated, the company takes on a legal persona which is separate and distinct from its owners and directors.

This concept of a separate legal entity is critical as it means that corporate control and ownership are separate in the sense that the power to manage the business of the company resides with the directors and that power has been expressly carved out by statute (section 157A of CA). The powers exercised by directors are exercised by directors as a collective body where their decisions are expressed by board resolutions.

Given that the balance of powers is unequivocally tipped in favour of the directors and the relative difficulty of shareholders to directly (save for the exercise of their vote at shareholder meetings or initiating shareholder litigation) intervene in the day-to-day decisions of a company, directors are therefore understandably subjected to onerous duties and responsibilities.

The importance of requiring accountability from directors was perhaps most aptly described more than five (5) decades ago in the case of *Canadian Aero Service Ltd v O'Malley* [1974] SCR 592 where the Supreme Court of Canada observed;

“strict application against directors ... is simply recognition of the degree of control which their positions give them in corporate operations, a control which rises above day-to-day accountability to owning shareholders and which comes under some scrutiny only at annual general or at special meetings. It is a necessary supplement, in the public interest ... an acknowledgement of the importance of the corporation in the life of the community and of the need to compel obedience by it and by its ... directors ... to norms of exemplary behaviour.”

Personal Liability and Exposure

In addition to duties imposed on directors by law, the fact that directors operate at the forefront of the company's operations renders them natural (and convenient) "targets" when deals turn sour or commercial decisions go awry. Directors can face personal exposure in a variety of circumstances, some more obvious than others. We cover some of these situations below:-

(1) **Breach of Directors Duties**. - Directors owe fiduciary duties and duties of care, skill and diligence to the company. A breach of the same exposes a director personally not only to claims for financial compensation but also to potential criminal penalties under section 157 of the CA (including fines, imprisonment terms or both). Such duties require directors to:

- a. to act honestly and in good faith in the best interests of the company ("best interests" factors those of the company's creditors when the company is in financial distress);
- a. not to exercise his powers for an improper purpose such as to profit personally from his office; and
- a. not to place himself in a position which will result in a conflict of interest between his duties to the company and his personal interests.
- a. take reasonable steps to place oneself in a position to guide and monitor the management of the company. To this end, a director cannot be a "sentinel asleep at his post" but is not expected to be "a forensics investigator or a sleuth, unless there are signs that would put him on inquiry".
- a. Notably, in relation to section 157(1) offences, the custodial threshold will be presumptively crossed and the onus will be on the director to convince the court otherwise.

(2) **Piercing of the corporate veil** (or "lifting the veil"). -- In Singapore, in "exceptional" situations, a court may choose to ignore the separate legal personality of a company and look to the members or the controllers of the company to hold them personally responsible for a liability that would otherwise have been the company's. For a court to pierce the corporate veil, a claimant must establish at least one of the following recognised grounds:-

- a. the justice of the case requires it;
- b. the court is called upon to exercise an equitable or analogous discretion;

- c. a company is employed to evade his controller's legal obligations;
- d. it is necessary to give effect to the legislative purpose of a statute;
- e. a company is employed as an agent or alter ego of its controllers;
- f. a company is a sham or façade;
- g. a director has procured or directed the company's commission of a tort;
- h. a company is employed to commit fraud.

(3) **A director's liability for his company's breach of contract.** -- Directors may also potentially be held personally liable for the company's breach of contract. There are three (3) possible scenarios where such personal exposure may arise for a director.

- a. Tort of procurement of breach of contract -- the director induces or procures his company to breach its contract with a third party.
- a. Unlawful means conspiracy as between the directors -- where directors conspire to procure their company to breach its contract. The underlying unlawful means would be the tort of inducement of breach of contract,
- a. Unlawful means conspiracy as between a director and his company -- where the director conspires with the company to cause the company to breach the contract.
- a. However, directors are exempt from personal liability "if their acts, in their capacity as directors, are not in themselves in breach of any fiduciary or other personal legal duties owed to the company"

(4) **Shareholder litigation (section 216 of the CA).** -- Directors may also find themselves embroiled / sandwiched in claims brought by minority shareholders for oppressive conduct. Whilst such scenarios typically involve concurrent allegations of directors also breaching their duties as directors, there is technically no need to find that the director breached his or her fiduciary or statutory duties to establish oppression. The lodestar of establishing oppression is the finding of commercially unfair conduct. For instance, the lawful termination of the employment of a CEO (e.g. concurrently a minority shareholder and perhaps also a board member) in accordance with the notice provisions of his or her employment contract may per se not constitute wrongful termination but nonetheless be found to form part of the oppressive conduct of the ruling majority to unfairly prejudice and silence a minority shareholder.

(5) **Regulatory exposure**. – The most obvious exposure that directors face are those that are expressly imposed by statute. What is less obvious is the extent of such liability given that these obligations are spread across various sector specific legislation. The following table demonstrates this (non-exhaustive):-

[See ANNEX A]

Director Protections

The Singapore courts and regulators, however, are equally sensitive to the fact that “A company provides a vehicle for limited liability and facilitates the assumption and distribution of commercial risk” and that “Undue legal interference will dampen, if not stifle, the appetite for commercial risk and entrepreneurship”.

In our next article, our directors will discuss the business judgment rule, D&O liability insurance and whether there are any constraints on the company indemnifying directors in respect of liabilities incurred in their professional capacity.

ANNEX A

Statute	Provision	Statutory duty	Penalty for non-compliance
Companies Act 1967	s 156	Every director or chief executive officer of a company who is in any way, whether directly or indirectly, interested in a transaction or proposed transaction with the company must as soon as is practicable after the relevant facts have come to his or her knowledge, disclose the same	Civil liability and criminal liability: fine up to S\$5,000, imprisonment up to 12 months, or both (s 156(15)).
Companies Act 1967	s 157(1)	Act honestly in the discharge of directors' duties.	Civil liability to account for profits or compensate the company; criminal liability: fine up to S\$20,000, imprisonment up to 12 months, or both (s 157(3)).
Companies Act 1967	s 157(1)	Exercise reasonable diligence in the discharge of directors' duties.	Same as above.
Companies Act 1967	s 157(2)	Do not improperly use your position to gain an advantage for yourself or another person or to cause detriment to the company.	Civil liability and criminal liability under s 157(3).
Companies Act 1967	s 157(2)	Do not improperly use information acquired as a director.	Civil liability and criminal liability under s 157(3).
Companies Act 1967	s 199	Ensure proper accounting records are kept and retained.	Civil liability and criminal liability: fine up to S\$10,000, imprisonment up to 12 months, or both (s 199(6)).
Companies Act 1967	s 201	Ensure financial statements are prepared in compliance with the Act and give a true and fair view.	Fine and/or imprisonment (s 203 / s 204).
Companies Act 1967	ss 175 & 197	Ensure Annual General Meetings are held where required and financial statements are laid before members.	Fine for default.
Companies Act 1967	s 401	To not knowingly give false or misleading information in any documents to ACRA	Fine up to \$50,000, imprisonment up to two years, or both.
Insolvency, Restructuring and Dissolution Act 2018	s 239	Do not engage in wrongful trading.	Personal liability, criminal fine and/or imprisonment.
Insolvency, Restructuring and Dissolution Act 2018	s 238	Do not carry on business with intent to defraud creditors (fraudulent trading).	Civil liability, criminal fine, imprisonment and possible disqualification.
Securities and Futures Act 2001	Various	Comply with disclosure obligations and avoid insider trading and market misconduct.	Civil penalties, criminal fines, imprisonment and disqualification.
Income Tax Act 1947	Various	Ensure company tax compliance.	Tax penalties, fines and prosecution.
Goods and Services Tax Act 1993	Various	Ensure GST compliance.	Financial penalties and prosecution.
Workplace Safety and Health Act 2006	s 48	Exercise due diligence where offences by the company are attributable to directors' consent, connivance or neglect.	Fine and/or imprisonment.

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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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