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Quis Custodiet Ipsos Custodes?[1] Being a mere legal entity, a company is unable to enforce its rights when they have been violated. For the company, its officers are the guardians protecting it. But what happens when the guards themselves are the wrongdoers? This is a pertinent issue here, given that Singapore-listed companies have recently been found wanting in corporate governance issues.[2]

In 1993, statutory derivative actions ("SDA") were introduced in the form of s 216A of the Companies Act ("CA")[3] to enforce the ideals of minority shareholders protection and managerial accountability.[4] It is with this aim in mind that the Steering Committee ("SC") made a few recommendations as regards s 216A in its recent report.[5] Accordingly, the SC would mainly be concerned with corporate governance when making the recommendations, given that it could affect investors' confidence and thus Singapore's economy. Hence, this paper will focus on how the recommendations can enforce corporate governance by deterring potential wrongdoers.

[1] Literally translated as "Who will guard the guards themselves?"
[2] Jamie Lee, "Where firms are found wanting in corporate governance issues", Business Times (15 March 2012), Available on Singapore Law Watch website <http://www.singaporelawwatch.sg/slw/headlinesnews/5887-where-firms-are-found-wanting-in-corporate-governance-issues.html?utm_source=email%20subscription&utm_medium=email> (accessed 15 March 2012).
[3] Companies Act (Cap 50, 2006 Rev Ed). Note that all provisions mentioned will be from the Companies Act (Singapore) unless expressly mentioned otherwise.
[4] George Shenoy and Pearlie Koh, "Company Law in Asia" (1997) 16 *Asia Business Law Review* 27, at page 31.
[5] *Consultation on the Report of the Steering Committee for Review of the Companies Act*, June 2011. The SC considered the purpose of SDA when it took into account the opinions mentioned at paragraph 147 of the report.

I. Recommendation 2.28.

A. Are SDA arbitrable?

The underlying premise for the following arguments is that SDA are arbitrable, for it would be illogical to recommend that s 216A be extended to arbitrations if otherwise. It is submitted that this premise is plausible, for the court in *Re Salomon Inc.* accepted that derivative suits are arbitrable.[6]

B. S 216A should be expanded to include arbitrations

(1) The current remedies are not perfect.

Although the SC is concerned that "shareholders will have no recourse" if the company's contracts provide for arbitration,[7] this is not entirely true. Remedies that shareholders could currently avail to were mentioned in *Kiyue Co Ltd v Aquagen International Pte Ltd* ("*Kiyue*"),[8] with one of them being the setting aside of the arbitration award.[9] Hence, there are existing remedies that can reverse the damage to the company.

Another remedy, albeit a contentious one, is for the shareholder to apply for a remedy under s 216. Should he succeed, the court could cancel or vary the arbitration award under s 216(2)(a) or allow for civil proceedings to be brought on behalf of the company under s 216(2)(c),[10] which is arguably possible given the wide range of powers that the court has.[11] That said, as s 216 has been commented as being inappropriate for seeking a relief primarily

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[6] *Re Salomon Inc. Shareholders' Derivative Litigation* No. 91 Civ. 5500 (RPP), 68 F.3d 554, at 557

[7] *Supra* n 5, at 141.

[8] *Kiyue Co Ltd v Aquagen International Pte Ltd* [2003] 3 SLR(R) 130, at [10].

[9] *Ibid.*

[10] It should be noted that Singapore Courts have allowed corporate relief to be granted in s 216 petitions, instead of giving leave to the petitioner to bring an action in the name of the company under s 216(2)(c). Such an order was given in the case of *Kumagai Gumi Co Ltd v Zenecon Pte Ltd and others and other appeals* [1995] 2 SLR(R) 304, where the court ordered the compressor to compensate the company.

[11] Pearlie Koh Ming Choo "The Statutory Derivative Action in Singapore – A Critical and Comparative Examination" (2001) *Bond Law Review*: Vol. 13: Issue 1, Article 3 at 87, where she mentioned that the courts are given wide powers under the provision.

benefitting the company,[12] shareholders would likely be unwilling to rely on such a contentious remedy.

Meanwhile, a shareholder could apply for leave to commence a SDA against errant directors under s 216A and for the arbitration proceedings to be suspended until the SDA has been adjudicated upon. While such an order is not expressly provided for in the CA, this is possible as s 216A(5) allows the Court to make interim orders that it thinks fit in the interests of justice.

However, though it is not entirely true that shareholders will have no recourse, the practical effects of the current remedies might not be fully in line with the focus of SDA.[13] Should a shareholder pray for a remedy via the above-mentioned avenues, the aggrieved shareholder would incur greater costs as he would have to undergo court proceedings before he can intervene in the arbitration. While the shareholder can be reimbursed for the legal costs in s 216A proceedings, this merely transfers the burden to the company. With the objective of a derivative action being the welfare of the company,[14] it is thus arguable that expanding s 216A to cover arbitrations would better fulfil the object of derivative actions since it streamlines the process and allows for the enforcement of the company's rights while incurring lower legal fees.

In conclusion, keeping in mind the purpose of introducing SDA,[15] it would appear that not expanding s 216A to arbitrations due to the existence of alternate remedies is simply a case of missing the woods for the trees.

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[12] *Walter Woon on Company Law* (Tan Cheng Han SC gen ed) (Sweet & Maxwell, 3rd Rev Ed, 2011) at para 9.92.
[13] Pearlie MC Koh, "The Statutory Derivative Action in Singapore" (1995) 7 S.Ac.L.J. 74 at 81. She mentions that "the focus of any derivative action… is the welfare or interests of the company as a whole."
[14] *Ibid*.
[15] *Supra* n 4.

(2) Other Jurisdictions

At this juncture, it is pertinent to note that most jurisdictions have not restricted SDA to apply only to court proceedings. In the United Kingdom, s 261 of the Companies Act allows for applicants to bring a derivative claim.[16] Meanwhile, Scotland and New Zealand provisions prefer to use the word "proceedings".[17] It is arguable that these provisions providing for SDA would include arbitration proceedings. After all, derivative claims can be made via arbitration, and the term "proceedings" is wide enough include arbitration proceedings as well. The latter proposition as regards "proceedings" can be proved by taking a comparative approach to Hong Kong's Companies Ordinance, which explicitly defines proceedings to those "within the jurisdiction of the court".[18] Accordingly, it can be inferred that without any explicit definition of "proceedings", the term is wide enough to encompass arbitration proceedings as well.

In addition, the Canadian provision for SDA arguably covers arbitrations though the term used here is "action",[19] which is identical to the term used in s 216A(2). In *Kiyue*, Justice Choo mentioned that there is a need to give the term a consistent meaning, and seeing that the CA discriminates between action and an arbitration proceeding, "action" is restricted to court proceedings.[20] It is submitted that as the Canada Business Corporations Act ("CBCA"), unlike the CA, does not make any reference to arbitration, it is thus arguable that a SDA via the CBCA includes arbitrations.

The *raison d'etere* in having SDA is likely to be the same across all jurisdictions and it has been shown that most jurisdictions do not exclude arbitration from SDA. Accordingly, it is

[16] Companies Act 2006 (c 46) (UK). S 261 is applicable to England and Wales and Northern Ireland.
[17] For New Zealand: Companies Act 1993 (1993 No 105, 2011 Reprint) (New Zealand) s 165. For Scotland: Companies Act 2006 (c 46) (UK) s 266.
[18] Companies Ordinance (c 32) (Hong Kong) s 168BA.
[19] Canada Business Corporations Act (R.S.C., 1985, C. C-44) (Canada) (caa 7 February 2012) s 239.
[20] *Supra* n 8, at [7].

arguable that Recommendation 2.28 would bring Singapore in line with other jurisdiction and thus better meet the object of s 216A.

(3) Plausible Concerns

(a) Frivolous applications

A common concern with SDA is the possibility of frivolous applications by disgruntled shareholders.[21] However, unmeritorious cases will be sifted out by the preconditions in s 216A.[22] Furthermore, the court's approval is required before discontinuing an action commenced under s 216A.[23] Such measures have been recognised to be capable of preventing an abuse of the system.[24] Hence, the current safeguards will continue to be sufficient, regardless of whether the application is regarding arbitration or court proceedings.

(b) Potential conflict with arbitration laws.

While it is not within the scope of this paper to examine arbitration laws, should the arbitration be considered as an international arbitration, "court intervention is limited and restricted to instances expressly provided by law."[25] Accordingly, it is arguable that accepting Recommendation 2.28 might result in a conflict with arbitration laws. However, this is not the SC's concern since the onus is on the shareholder's solicitors to consider any potential conflict of laws before applying to the courts to grant leave under s 216A.

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[21] This problem was discussed in the Parliament when s 216A was first introduced. See *Singapore Parliamentary Debates, Official Report* (14 September 1992) vol 60 at cols 252–253 (Dr Richard Hu Tsu Tau, Minister for Finance). The concern of s 216A inviting unnecessary litigation due to frivolous applications was brought up by Ms Susan de Silva as well in *Report of the Select Committee on the Companies (Amendment) Bill (Bill No. 33/92)* (Parl. 2 of 1993, 26 April 1993) at B10.

[22] *Supra* n 11, at 72–73.

[23] See s 216B(2).

[24] Low Kee Yang, "Minority Shareholder Protection: Major Changes Under Singapore Law" (1994) 3 *Asia Business Law Review* 90, at 91.

[25] Lawrence Boo, An Overview of the Singapore Legal System, Chapter 4 – International and Domestic Arbitration in Singapore, at 4.1.2, <http://www.singaporelaw.sg/content/arbitration1.html#Section2> (accessed 28 February 2012).

The pertinent issue here is that different jurisdictions have different thresholds in granting leave for a SDA. Hong Kong, for example, arguably has a lower threshold since it does not expressly require the applicant to be acting in good faith.[26] Hence, if the governing law in the arbitration is that of Hong Kong, should the court decide to grant leave according to the preconditions in s 216A?

In conclusion, though the recommendation is definitely a step in the right direction, the SC might wish to further examine the potential conflict with arbitration laws, given that Singapore aspires to be an arbitration hub and any uncertainty resulting from conflicts with arbitration laws would affect this aspiration.

II. Recommendation 2.29

This recommendation is closely linked to Recommendation 2.30 since it will be met if the latter is accepted. Hence, the underlying assumption is that of Recommendation 2.30 being rejected, though, as will be seen later, there are good reasons to adopt it.

A. The artificial distinction.

In the event that s 216A is not extended to companies listed locally, it should not be made available to companies listed overseas as well, seeing that the reasons for not allowing an SDA would apply to both groups.

Firstly, shareholders of all listed companies are generally able to sell their shares. Thus, it is odd that the distinction between the two groups of companies was made on the basis that "disgruntled shareholders… can sell their shares".[27] Another reason offered by the SC when s 216A was first introduced was that the companies listed locally are "already monitored by

[26] Companies Ordinance (c 32) (Hong Kong) s 168BC.
[27] *Supra* n 11, at 81.

various regulatory authorities",[28] and can thus be excluded. With all due respect, such a distinction is asinine. Companies listed overseas will, likewise, have to comply with regulatory authorities ("regulators") abroad. For instance, companies listed in Australia have to comply with the Australian Securities and Investment Commission ("ASIC"), which has been noted for being proactive in enforcing corporate governance.[29] However, despite ASIC's enforcement, SDA is available to all listed companies.[30] Hence, there is no reason in differentiating between groups of listed companies as regards the availability of SDA.

B. The inconsistency might result in uncertainty for cases of dual listings.

The report mentioned that "[o]ne of SGX's policies is to promote dual listings".[31] With some 'creative lawyering', this policy might give rise to some uncertainty should there be inconsistency in the availability of SDA to listed companies. In the event that a Singapore-incorporated company is listed overseas and in Singapore, there might be arguments that the s 216A application is made in the capacity of a company listed overseas, not that of a locally listed company. This argument, if accepted, would make the distinction otiose and might affect the certainty of the law in this regard, possibly giving potential investors pause in considering whether to invest in the first place.

Accordingly, it is submitted that there should be consistency as regards the availability of SDA to all listed companies.

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[28] *Ibid*.
[29] Brian R. Cheffins & Bernard S. Black, "Outside Director Liability Across Countries" 84 TXLR 1385, at 1438. While the article is about derivative actions against non-executive directors, the arguments put forth are applicable to errant directors in general.
[30] Corporations Act 2001 (Act No. 50 of 2001) (Australia) s 236.
[31] *Supra* n 5, at 144.

III. Recommendation 2.30

A. S 216A should have been made available to all companies.

S 216A's controversial exclusion of listed companies should never have occurred,[32] given that the reasons given were flawed. Furthermore, in all of the jurisdictions examined,[33] no provision for SDA excluded its applicability to listed companies on the local exchange. In fact, a New Zealand commentator observed that SDA should be the "major legal control in the public company."[34] Accordingly, the writer argues that the exclusion goes against the overarching objective of SDA, which is to enhance corporate accountability by increasing the scope for shareholder intervention. Hence, it is submitted that s 216A should never have excluded listed companies.

(1) Presence of regulators and common law derivative action.

While the work of regulators in deterring mismanagement does reduce the need for SDA, relying heavily on them is not a perfect answer to corporate management.[35] An overly intrusive regulator will affect the commercial attractiveness of a market,[36] and this would undoubtedly affect Singapore's economy. Furthermore, regulators will not be able to pursue every breach of duty.[37] This would exacerbate the shareholder's problems; for he is left with no effective legal recourse if the regulators choose not to intervene.

In the meantime, though minority shareholders can pursue a common law derivative action ("CLDA"), the difficulties in using this avenue was the reason for enacting s 216A in the first place. Hence, excluding listed companies because they have a remedy via CLDA is

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[32] *Supra* n 24, where the author described the move to exclude listed companies as a controversial one.
[33] The jurisdictions are Australia, Hong Kong, New Zealand, United Kingdom and Canada.
[34] G. Shapira, "Minority Buy-outs and Derivative Actions in New Zealand" paper presented at the 1994 National Corporate Law Teachers Conference, UTS Sydney.
[35] *Supra* n 13, at 85.
[36] Margaret Chew, "The Securities Regulator in Civil Pursuit" 1999 SINGJLS 596 at 605–606.
[37] I Ramsay, "Corporate Governance, Shareholder Litigation and the Prospects for a Statutory Derivative Action" (1992) 15 UNSWLJ 149 at 152.

contradictory with the purpose of introducing s 216A. Furthermore, as was mentioned earlier, s 216 is not a truly viable option. These only serve to reinforce the conclusion that having regulators and CLDA do not justify the exclusion of listed companies.

(2) The ability of shareholders to sell their shares.

Although disgruntled shareholders can opt for a quick exit by selling their shares, the truth is that as a result of corporate mismanagement, shareholders are likely to be unable to sell the shares without incurring a loss.[38] While shareholders can pray for a buy-out order, this would do little to enhance managerial accountability.[39] It is thus submitted that an exclusion based on this justification runs counter to the *raison d'etere* of s 216A's enactment in the first place.

Accordingly, s 216A should have been applicable to listed companies since its introduction.

B. Reasons to extend s 216A

A recent study has found Singapore-listed companies to be wanting in corporate governance issues.[40] Seeing that s 216A has been found to be an effective deterrent to corporate mismanagement,[41] there is *prima facie,* a strong case in extending s 216A to them, even if it is just to deter potential wrongdoers. It is likely that in making this recommendation, the SC is seeking to enforce corporate mismanagement by way of deterrence since it is inadvisable to over-interfere in companies. It is submitted that extending s 216A provides a strong deterrent against wrongdoing in listed companies.

[38] *Supra* n 35.
[39] *Ibid.*
[40] *Supra* n 2.
[41] *Supra* n 11, at 94.

(1) Shareholders are now likely to seek recourse via s 216A, making it an effective deterrent.

The strength of the provision's deterrent effect is dependent, *inter alia*, on the likelihood of a shareholder pursuing a SDA.[42] Seeing that any awards will benefit all share-holders pro rata while the applicant has to risk hefty legal costs,[43] it is likely that shareholders will be deterred from pursuing derivative actions.[44] This would lower the deterrent effect of s 216A.

However, the argument above has been weakened by later events. Singaporean shareholders have formed an unofficial 'watchdog' for minority rights.[45] Thus, it is likely that these shareholders will be willing to bear the downside risk from losing, given that they can pool their resources together for a minority shareholder to commence a SDA to 'send a message' to wrongdoers. This undoubtedly increases the deterrent effect of s 216A if it is made available to listed companies.

In addition, the policy of attracting institutional investors arguably mandates the need for Recommendation 2.30.[46] The option of selling out is not a viable one for these investors,[47] and thus, the exclusion of listed companies would leave them with no recourse. Hence, extending s 216A to listed companies and providing minority shareholders with a legal recourse is necessary to attract institutional investors. Furthermore, should the recommendation be accepted, these investors will likely make use of s 216A as they have no

[42] *Supra* n 29.
[43] S 216A(5)(c) only applies when leave is granted. Hence, the applicant will have to bear the legal costs if leave is denied.
[44] *Supra* n 29, at 1407, where it was mentioned that "one final deterrent to derivative litigation… shareholder must bear the downside risk from losing to pursue an action that will benefit all shareholders pro rata."
[45] *Supra* n 11, at 83.
[46] *Ibid*, where it was mentioned that the Singapore Government has been encouraging the development of the funds management industry and this will result in a growing presence of institutional investors
[47] *Ibid*.

other recourse. Hence, an extension of the applicability of s 216A, coupled with the presence of institutional investors will deter corporate mismanagement.[48]

(2) Regulators using s 216A as a strong deterrent.

While shareholders are willing to enforce corporate governance via SDA, such actions can pose real risks to the company's reputation and result in doing more harm.[49] Hence, it is clear that regulators are needed, but as a complement instead of a substitute. Furthermore, it is submitted that regulators can only provide effective enforcement with the extension of SDA to listed companies.

Should Recommendation 2.30 be accepted, regulatory agencies may apply for SDA under s 216A.[50] Being civil actions with a lower standard of proof, the threat of being successfully sued under s 216A is more real as opposed to criminal prosecution, and an award of damages under a civil action could be much higher than any maximum fine.[51] This will result in the provision being a better deterrent against wrongdoing in listed companies.

Furthermore, allowing the regulator to commence SDA via s 216A would avail the regulator to a variety of orders or remedies that can prevent a wrongdoer from "dissipating monies or property with the aim of defeating any potential judgment."[52] This would further increase the deterrent effect of s 216A as it closes any loophole wrongdoers can exploit to escape the consequences of their misdeeds.

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[48] *Ibid*.
[49] *Supra* n 29, at 1467.
[50] S 216A(1)(c) allows for a regulatory agencies to be a complainant under the provision if the Court decides that it is a proper person to make an application under this section.
[51] *Supra* n 36, at 624.
[52] *Id*, at 625.

Hence, the prospect of a regulator bringing a SDA will be "a potent disincentive and deterrent for any aspiring offender",[53] as corporate officials will be aware that both shareholders and regulators can effectively take them to task for their wrongdoings with a variety of orders and remedies. Accordingly, extending the applicability of s 216A to listed companies would provide a strong deterrent effect and reinforce the purpose of introducing SDA in the first place. Thus, the SC is right in calling for the extension of s 216A to companies listed locally.

C. Allaying fears and concerns

A major concern in allowing SDA for listed companies is that of over-interference in the management of the company due to the fear of facing frequent litigation suits and this might result in capable, yet risk-adverse, persons to reject directorships.[54] In addition, there was the concern that the unscrupulous might attempt to manipulate share prices.[55] It is submitted that though there is merit in being concerned about opening the floodgates overly widely to shareholder litigation,[56] such fears are more perceived than real.

As mentioned earlier, the preconditions in s 216A will filter out unmeritorious cases.[57] Furthermore, it is unlikely for regulators to intervene in the management of the company unless there is a regulatory purpose to taking action.[58] That said, given the small pool of public company directors,[59] it is necessary for the SC to do more to allay such perceived fears to encourage capable persons to become directors and indirectly stimulate the economy. It is suggested that the SC can consider introducing provisions that will allow directors to claim damages from disgruntled shareholders should they apply for SDA wrongfully or without

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[53] *Ibid*.
[54] *Supra* n 11, at 85.
[55] *Supra* n 5, at 143.
[56] *Supra* n 54.
[57] *Supra* n 11, at 72–73.
[58] *Supra* n 36, at 629 where it was opined that unless "a regulatory purpose is identified, the securities regulator ought not to pursue an action simply because… many irate and impecunious investors have suffered loss."
[59] *Supra* n 54.

reasonable cause.[60] This will ensure that over-interference from shareholders will not ensue after extending s 216A to listed companies, allowing directors to focus on the company's development, which in turn boosts the economy.

IV. Concluding Opinions

In conclusion, the real question is: "who will *better* guard the guards?" It is submitted that the shareholders are the best candidates to prevent corporate mismanagement, for a company by itself is unable to enforce its own rights when the directors themselves are the wrongdoers. It is for this purpose that shareholders require more effective remedies they can turn to. Considering the overall effect of the three recommendations, potential wrongdoers will be deterred as they are watched by both shareholders and regulators (for listed companies), and cannot get off scot-free by having arbitration clauses. Seeing that s 216A is an effective deterrent and that there is a need for better corporate management in Singapore-listed entities, it is time for the provision to be extended to all listed companies. With better corporate governance and protection of shareholders' rights, investors will be attracted and this would in turn benefit the country's economy.

[60] The principles in deciding whether an application is wrongful, vexatious, or without reasonable cause can be derived from the courts deciding cases regarding s 128 of the Land Titles Act (Cap 157, 2004 Rev Ed), i.e. "Compensation payable for wrongfully lodging caveats, etc."