

## MAKING A CASE FOR THE DUTY TO ACT FOR PROPER PURPOSES

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The duty to act for proper purposes is seldom applied and thus is not well-developed in Singapore. The aim of this article is to describe the development of the duty to act for proper purposes in other Commonwealth jurisdictions, and in the process, better understand when an exercise of a power by a director may be subject to review according to the duty. The argument is made that the duty is flexible, capable of application in a wide variety of situations and it is hoped the law as regards this duty has the opportunity to develop in Singapore.

### I. INTRODUCTION

Lord Greene M.R. in *Re Smith and Fawcett, Limited* had described the directors' equitable duty as encompassing the duty to act "bona fide in what they consider—not what a court may consider—is in the interests of the company, and not for any collateral purpose."<sup>1</sup> This statement sparked a debate as to whether one or two duties were imposed on the director. It is generally accepted that the duty to act bona fide in the interests of the company and the duty to act for proper purposes are two distinct duties and, without going over well-trodden ground,<sup>2</sup> one of the premises of this article is that the duty to act for proper purposes is separate from and independent of the duty to act bona fide in the interests of the company. For the purposes of this article, the duty to act for proper purposes is a reference to the rule of equity that powers conferred on a director of a company—a fiduciary of the company—should be used only for the purpose(s) for which the powers were conferred on that fiduciary and not for any collateral purpose(s).

There is a dearth of authority in Singapore applying the duty to act for proper purposes. Because of this, it is probably correct to say that, in the Singapore context as has been said in the English context that, "[t]his rule is... the least discussed and

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<sup>1</sup> [1942] Ch. 304 at 306 (C.A.).

<sup>2</sup> See e.g., *Whitehouse v. Carlton Hotel Proprietary Limited* (1987) 162 C.L.R. 285 (H.C.A.) [*Whitehouse*]; *Hogg v. Cramphorn Ltd.* [1967] Ch. 254 (Ch.) [*Hogg*]; *Howard Smith Ltd. v. Ampol Petroleum Ltd.* [1974] A.C. 821 (P.C.) [*Howard Smith*]. See also Mok Cui Ling, "Rethinking Directors' Duties: An Analysis of the Proper Purpose Doctrine" (2002) 14 Sing. Ac. L.J. 387, where the author devoted considerable attention to the argument that the duty to act bona fide in the interests of the company and the duty to act for proper purposes are distinct duties.

least well understood of the fiduciary obligations affecting a director”.<sup>3</sup> This state of affairs is regrettable. The duty to act for proper purposes is important because it is a flexible and useful tool which enables the court to review the directors’ decisions. It is also important not least because certain developments in company law hint that the duty may gain ascendancy in the future. The aim of this article is to describe the development of the duty to act for proper purposes in other Commonwealth jurisdictions and, in the process, better understand when an exercise of a power by a director may be subject to review according to the duty.

The second and third sections of this article are structured around the two-step test laid down in *Howard Smith Ltd. v. Ampol Petroleum Ltd.*, the *locus classicus* on the duty to act for proper purposes. Lord Wilberforce laid down a two-step test to determine if a fiduciary has exercised a power for an improper purpose, stating the court is to:<sup>4</sup>

1. Ascertain as a matter of law the purposes for which the power may, and may not be exercised (“Step 1”); and
2. Determine as a matter of fact the purpose for which the power was exercised in the particular case and whether that power is within the category of permissible purposes (“Step 2”).

The second section of this article focuses on Step 1, which contends with the issue of how the court is able to ascertain, as a matter of law, the purposes for which the power may or may not be exercised. It would appear that the court considers the power-conferring provision, the nature of the company and the nature of the power in order to ascertain the standards to be expected of a director or a board in that situation. It is unfortunate that directors may never be fully confident that they are acting for proper purposes pursuant to Step 1 because it is for the court, not the director, to ascertain what the proper purposes are. However, there is something to be said about ensuring that the wide discretionary powers conferred on a director or a board are not to be exercised untrammelled on every occasion. Thus, short of abolishing wide discretionary powers, which is not workable because it is necessary to confer such powers on a director or a board, Step 1 strikes a delicate balance by allowing the court to rein in a director’s or a board’s exercise of discretionary power on a highly selective basis, by reference to the purposes for which the power is conferred on a director or a board in that particular case.

The third section of this article focuses on Step 2, which grapples with the issue of how the court is able to determine, as a matter of fact, the purpose for which the power is exercised in the particular case. There appears to be two strands of cases. One strand makes clear the bona fides of the director or the board is irrelevant to the court’s determination of the purpose for which the power was exercised. Another strand seems to take into account the bona fides of the director or the board and makes statements to the effect that the court will defer to the director or the board where they exercised that power bona fides in the interests of the company. Some attention

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<sup>3</sup> Richard C. Nolan, “The Proper Purpose Doctrine and Company Directors”, in Barry A.K. Rider, ed., *The Realm of Company Law: A Collection of Papers in Honour of Professor Leonard Sealy*, *SJ Berwin Professor of Corporate Law at the University of Cambridge* (London: Kluwer Law International, 1998) 1 at 1.

<sup>4</sup> *Howard Smith*, *supra* note 2 at 835.

will be given to untangling these two strands. It will be argued that for Step 2, the court should not be concerned with the *manner* in which the power was exercised, but rather with the *purpose* or the ends for which the power was exercised.

It will be seen in the fourth section of this article that the duty to act for proper purposes is flexible and capable of application in many situations. There is much room for the development of the duty as a critical tool to be used to review the directors' decisions.

## II. ASCERTAINING AS A MATTER OF LAW WHAT THE PROPER PURPOSES ARE

The first step, according to *Howard Smith*, is for the court to ascertain the purpose(s) for which a power was conferred so that the limitations within which the power may be exercised can be defined. On the face of it, the issue appears to be one involving the interpretation of the provision, usually the article, which confers the power. The process of interpretation may produce a positive result in that it may show a power was conferred for a particular purpose. It may also produce a negative result in that it may show the power cannot be used for certain specified purposes. The court in *Whitehouse v. Carlton Hotel Proprietary Limited* even went so far as to say that the provision may authorise the exercise of a power for what would ordinarily be an improper purpose.<sup>5</sup>

But the instances in which it is clearly spelt out in a provision that the power may be used for a purpose or may not be used for a purpose are likely to be exceptions rather than the rule. A review of the *Table A*<sup>6</sup> articles will reveal many powers conferred on directors<sup>7</sup> that do not state the purposes for which those powers were conferred. Many companies adopt the *Table A* articles, which means that, in the majority of cases, the purpose for which a particular power is conferred will not be spelt out. Thus, the court is compelled to consider matters extraneous to the power-conferring provision in order to ascertain the purposes for which the power was conferred.

The concept of looking *outside* the power-conferring provision to ascertain the purposes for which a power was conferred is not entirely new. In administrative law<sup>8</sup> and in equity pursuant to the doctrine of a 'fraud on power',<sup>9</sup> an exercise of discretion which went beyond the bounds ascertained by the courts would be declared to be outside the scope of the power. There may be concerns that the courts should not be making subjective value judgments about the purposes for which a power is conferred. Yet, discretionary powers are often drafted in extremely broad terms and if it were accepted that those who conferred the power on the fiduciary, although not having stated the purposes explicitly (because it is impossible to list down every purpose for which a power is conferred), they may have intended those powers to be curbed in situations where the fiduciary is acting disloyally. As such, intervention

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<sup>5</sup> *Supra* note 2 at 312, 313 (Brennan J.).

<sup>6</sup> Fourth Schedule of the *Companies Act* (Cap. 50, 2006 Rev. Ed. Sing).

<sup>7</sup> See *e.g.*, art. 13 on the power to make calls, art. 22 on the power to approve transfers, art. 30 on the power to forfeit shares, art. 68 on the power to appoint a person to be a director.

<sup>8</sup> See *e.g.*, *Associated Provincial Picture Houses Limited v. Wednesbury Corporation* [1948] 1 K.B. 223 (C.A.).

<sup>9</sup> See *e.g.*, *Vatcher v. Paull* [1915] A.C. 372 (P.C.).

by the courts to supplement the intention of those who conferred the power on the fiduciary may be defensible.

Ascertainment of the purposes for which the power was conferred thus often goes beyond the interpretation of the power-conferring provision and looks to facts specific to the company in order to place limits on the power. An important consideration is the nature of the company. Considering the nature of the company may mean that the court construes the power in the context of the business that the company is engaged in. In *The Australian Metropolitan Life Assurance Company Ltd v. Ure*,<sup>10</sup> the court had regard to the nature of the company as an insurance company and held that the power conferred on the board to refuse registration of a transfer of shares was given for the purpose of ensuring that insolvents and others whose reputations would damage the company's reputation were not admitted as members lest they become directors.<sup>11</sup>

Reflecting on the nature of the company could also mean construing the power in the context of the type of company—for instance, whether it is an exempt private company or a public listed company. Let us consider, for example, the power to register transfers. In an exempt private company, in deciding whether to exercise their powers to register a transfer, directors may consider many factors, such as whether the proposed transferee is a competitor of the company.<sup>12</sup> The power to register transfers, seen in the context of an exempt private company, may explain decisions such as *Re Smith and Fawcett, Limited*. In that case, the article conferred on the directors the discretion to admit new members. The company in question was a small closely-held one. The court read the article generously, as having conferred on the directors absolute discretion,<sup>13</sup> and produced an outcome in effect similar to that of admission of partners under partnership law.

In contrast, directors of a public listed company are not to be concerned with the identities of individual shareholders. While shares of such companies are freely transferable and that directors do not exercise the power to register transfers, they may, however, exercise other powers that affect shareholder control, for example, the power to issue shares. The tendency to exercise powers that affect shareholder control becomes more acute in a takeover situation.<sup>14</sup> The public listed company is governed by 'hard' and 'soft' rules, which include, *inter alia*, the *Securities and Futures Act*,<sup>15</sup> the *Companies Act*,<sup>16</sup> the *SGX-ST Listing Manual*<sup>17</sup> and the *Singapore Code on Take-overs and Mergers*.<sup>18</sup> Suppose the court is asked to determine if the board's exercise of its power to issue shares was in breach of the duty to act for

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<sup>10</sup> (1923) 33 C.L.R. 199 (H.C.A.).

<sup>11</sup> See *e.g.*, *ibid.* at 215-217 (Isaacs J.), 222 (Starke J.).

<sup>12</sup> *Re Bede Steam Shipping Company, Limited* [1917] 1 Ch. 123 (C.A.); *Charles Forte Investments Ltd. v. Amanda* [1964] Ch. 240 (C.A.).

<sup>13</sup> *Supra* note 1 at 308.

<sup>14</sup> See *e.g.*, *Punt v. Symons & Co., Limited* [1903] 2 Ch. 506 (H.C.); *Hogg v. Cramphorn Ltd.*, *supra* note 2; *Howard Smith Ltd.*, *supra* note 2.

<sup>15</sup> Cap. 289, 2006 Rev. Ed. Sing.

<sup>16</sup> *Supra* note 6.

<sup>17</sup> Online: Singapore Exchange <<http://rulebook.sgx.com/>> [Listing Manual]. It is an amalgamation of the Mainboard Rules and the Catalist Rules.

<sup>18</sup> Online: Monetary Authority of Singapore <[http://www.mas.gov.sg/~media/resource/sic/Take\\_over\\_Code\\_9\\_Apr\\_2012.pdf](http://www.mas.gov.sg/~media/resource/sic/Take_over_Code_9_Apr_2012.pdf)> [Takeover Code].

proper purposes. It should not be a stretch to argue that the *Listing Manual, Takeover Code* and the decisions of the Securities Industry Council may possibly provide the backdrop to help understand the expectations of those who invest in such companies, and thus assist the court in ascertaining the purposes for which the power to issue shares have been granted to the board. It is not suggested that the courts should declare a purpose as proper or improper because the Securities Industry Council had made a ruling on a similar issue earlier. It is suggested that when the court looks outside the power-conferring provision to ascertain the proper purposes for which a power was conferred, it should consider the nature of the particular company in question in the context of the 'hard' rules, 'soft' rules and even norms that govern it in order to discern the purposes for which the power was conferred. Indeed, looking to extraneous rules and norms is not unfair to the director or board in question because these rules and norms influence and shape the standards expected of a fiduciary office holder in the particular situation. It must, after all, be remembered that the power was conferred on a director or a board in his capacity as a fiduciary. The director or board in question is merely being held to standards defined by the expectations of those who invest in this type of company and even the expectations of the director or board themselves.

The English High Court and Court of Appeal have had the opportunity to consider these extraneous factors in the application of the duty to act for proper purposes in *JKX Oil & Gas Plc v. Eclairs Group Ltd.*<sup>19</sup> Section 793 of the *Companies Act 2006* permits a company to send notice to any person whom it knows or has reasonable cause to believe is interested in the company's shares in order to seek information about that person's interests.<sup>20</sup> Article 42 of the company's ("JKX Oil") articles of association set out restrictions that it itself could impose on a person failing to give that information. Mann J. in the High Court was clear that JKX Oil's board had, in deciding to impose the voting restrictions, acted for improper purposes. The purpose was to improve the prospects of the board's resolutions being passed at the general meeting, rather than to compel the provision of information requested in the s. 793 notices. On a majority 2-1 judgment, the Court of Appeal overturned the High Court's decision. In the lower court, Mann J. had considered the purpose of s. 793 and concluded that the restrictions imposed under art. 42 of the company's articles had to be for the purpose of eliciting information pursuant to that section. The majority of the Court of Appeal, on the other hand, considered that since the *2006 Act* does not specify that the sanction of restrictions on voting can only be imposed for any particular purpose, the duty to act for proper purposes had no significant place in the operation of Part 22 of the *2006 Act*. Although there is a difference in opinion as to the purpose of s. 793 between the High Court and the majority of the Court of Appeal, it is clear that both courts, in analysing the power of the board of JKX Oil to impose restrictions under art. 42 of the company's articles, had recourse to extraneous rules outside of the articles and considered the broader context of Part 22 of the *2006 Act* which also governed the company. It can be seen that it is extremely difficult to ascertain the purpose for which a power is conferred on the board and looking to extraneous rules does not make the task of the court easier. Leave to

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<sup>19</sup> [2013] EWHC 2631 (Ch) and [2014] EWCA Civ 640 respectively.

<sup>20</sup> *Companies Act 2006* (U.K.), 2006, c. 46 [2006 Act].

appeal for the Court of Appeal's ruling has been granted and it remains to be seen if the Court of Appeal's robust approach to the duty to act for proper purposes will be upheld.

In addition to considering the nature of the provision, Professor Nolan has argued that the court should consider the nature of the power conferred on the director or board in terms of the powers that are exercised internally (those that directly impact members or members *vis-à-vis* each other) as well as powers that are exercised externally (those that impact third parties dealing with the company).<sup>21</sup> Professor Nolan has observed that the courts subject the exercise of internal powers to greater scrutiny than the exercise of external powers because powers that are exercised externally, for example, the power to sell an asset to a third party, tend to be managerial decisions which the courts are reluctant to interfere with.<sup>22</sup>

While Professor Nolan's categorisation of internal and external powers could explain some of the varying judicial approaches to the directors' exercise of powers, the distinction is not without its difficulties. First, it is not clear that there is a dichotomy between internal and external powers. An exercise of an internal power, for example, the power to decide on the quantum of dividend, directly impacts both members and the business of the company (the latter in terms of the investment capabilities of the company). It will thus be hard to explain a court's laxity or stringency in scrutinising a decision on the basis that the court should be more lax because this is a commercial decision that impacts the company or more stringent because this is a decision that impacts the shareholders.

Second, it is hard to discern a common thread that runs through the cases using the internal-external powers dichotomy. For every situation concerning, say, an internal power such as the power to issue shares, one will find a 'stringent' court decision<sup>23</sup> where the court invalidated the share issue on the basis that the board issued shares to upset shareholder control within the company, but he will also find a 'lax' court decision<sup>24</sup> where the court defers to the management's decision. An example of the latter is *Teck Corporation v. Millar*.<sup>25</sup> In that case, Teck held a majority shareholding in Afton Mines Ltd. ("Afton"), which held valuable mineral rights. Teck indicated its intention to replace the Afton board and then make an agreement with Afton for Teck to exploit the mineral rights. Before this could be done, and in order to prevent it, the directors of Afton made an exploitation agreement with Canadian Exploration Ltd. ("Canex"), providing for an issue of shares to Canex which would displace Teck's majority. Berger J. found that the directors' purpose was to "obtain the best agreement" they could for realising the company's assets while they were in control.<sup>26</sup> This was considered a legitimate purpose, even though an integral part of the scheme was that Teck's majority would be displaced by the issue of shares.

Although the author has certain reservations about the internal-external powers analysis, it would be logical for the court to examine the nature of the provision. It is submitted that the court should, instead, take into account the 'larger' context in

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<sup>21</sup> *Supra* note 3 at 23 *et seq.*

<sup>22</sup> *Ibid.* at 25.

<sup>23</sup> See *e.g.*, *Howard Smith*, *supra* note 2.

<sup>24</sup> See *e.g.*, *Teck Corporation v. Millar* (1973) 33 D.L.R. (3d) 288 (B.C.S.C.).

<sup>25</sup> *Ibid.*

<sup>26</sup> *Ibid.* at para. 156.

which the provision was found, in order to understand the nature of the provision. In the case where it is an article that confers the power, the company's memorandum and articles as a whole (as opposed to just the power-conferring provision) should be examined to understand the nature of the power. In *Howard Smith*, the nature of the provision which conferred on the board the power to issue shares was understood in the context of how the constitutional arrangements of that company were to operate in practice—namely, the power to issue shares was not to be exercised to upset the balance of power between the board and the members as understood within that company. Lord Wilberforce explained it as follows:<sup>27</sup>

The constitution of a limited company normally provides for directors, with powers of management, and shareholders, with defined voting powers having to appoint the directors, and to take, in general meeting, by majority vote, decisions on matters not reserved for management. Just as it is established that directors, within their management powers, may take decisions against the wishes of the majority of shareholders, and indeed that the majority of shareholders cannot control them in the exercise of these powers while they remain in office... so it must be unconstitutional for directors to use their fiduciary powers over the shares in the company purely for the purpose of destroying an existing majority, or creating a new majority which did not previously exist. To do so is to interfere with that element in the company's constitution which is separate from and set against their powers.

In *Equitable Life Assurance Society v. Hyman*,<sup>28</sup> art. 65 of the company's articles of association gave the directors a wide discretionary power to pay bonuses on its members' life assurance policies, and in the exercise of this power, the directors gave some policyholders larger bonuses than others. In this case, the House of Lords read art. 65 in the context of certain 'guarantees' that were given when certain of the members took out their policies and cut down the scope of discretion granted to the directors pursuant to art. 65.<sup>29</sup> Lord Steyn explained his decision in the following manner:<sup>30</sup>

The inquiry is entirely constructional in nature: proceeding from the express terms of article 65, viewed against its objective setting, the question is whether the implication [*i.e.* that the directors would not exercise their discretion in a manner which deprived the guarantees of substantial value] is strictly necessary... In this context the self-evident commercial object of the inclusion of guaranteed rates in the policy is to protect the policyholder against a fall in market annuity rates by ensuring that if the fall occurs he will be better off than he would have been with market rates. The choice is given to the GAR policyholder and not to the Society. It cannot be seriously doubted that the provision for guaranteed annuity rates was a good selling point in the marketing by the Society of the GAR policies. It is also obvious that it would have been a significant attraction for purchasers of GAR policies. The Society points out that no special charge was made for the

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<sup>27</sup> *Howard Smith*, *supra* note 2 at 837.

<sup>28</sup> [2002] 1 A.C. 408 (H.L.) [*Equitable Life Assurance*].

<sup>29</sup> *Ibid.* at 459.

<sup>30</sup> *Ibid.*

inclusion in the policy of GAR provisions. So be it. This factor does not alter the reasonable expectations of the parties. The supposition of the parties must be presumed to have been that the directors would not exercise their discretion in conflict with contractual rights. These are the circumstances in which the directors of the Society resolved upon a differential policy which was designed to deprive the relevant guarantees of any substantial value. In my judgment an implication precluding the use of the directors' discretion in this way is strictly necessary. The implication is essential to give effect to the reasonable expectations of the parties.

It would appear that the courts pay attention to the nature of the provision and construe it in the 'larger' context of expectations within the company—in *Howard Smith*, it was expectations as to how the division of powers between the board and members was to operate within that company and in *Equitable Life Assurance Society*, it was the expectations of the members evidenced by the policies that they had purchased.

It may be seen that in construing the power-conferring provision, the court does not merely interpret the words of the provision, but construes it in the context in which the provision appears, taking into account the nature of the company and the nature of the provision.

### III. ASCERTAINING AS A MATTER OF FACT WHAT THE ACTUAL PURPOSE IS

Step 2 requires the court to determine the actual purpose of a particular exercise of power. This aspect of the analysis is also not without its difficulties.

First, in finding out whether a power has been exercised for a proper purpose, it is necessary to determine the collective purpose of the board. If it is difficult to ascertain the purpose of an individual's act, it is more difficult to ascertain the collective purpose of the board. According to *Harlowe's Nominees Pty. Limited v. Woodside (Lakes Entrance) Oil Company No Liability*,<sup>31</sup> the court may have to ascertain the substantial purpose of the majority directors, even though the majority of the majority may turn out to be a minority of the whole board.<sup>32</sup> Second, even if it is possible to ascertain the collective purpose of the board, this may be inhibited by the fact that the board may have multiple purposes. According to *Howard Smith*, the court will determine if the *substantial* purpose was a permissible purpose.<sup>33</sup> However, the court in *Whitehouse* favoured a narrower approach. Mason, Deane and Dawson JJ., speaking on the exercise of power to issue shares, established a 'but-for' test instead.<sup>34</sup>

In this Court, the preponderant view has tended to be that the allotment will be invalidated only if the impermissible purpose or a combination of impermissible purposes can be seen to have been dominant – 'the substantial object'... As a matter of logic and principle, the preferable view would seem to be that, regardless of whether the impermissible purpose was the dominant one or but one of a number of significantly contributing causes, the allotment will be invalidated if

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<sup>31</sup> (1968) 121 C.L.R. 483 (H.C.A) [*Harlowe's Nominees*].

<sup>32</sup> See *e.g.*, *ibid.* at para. 18.

<sup>33</sup> *Supra* note 2 at 832.

<sup>34</sup> *Supra* note 2 at 294.

the impermissible purpose was causative in the sense that, but for its presence, “the power would not have been exercised”: per Dixon J., *Mills v. Mills*...

It is possible that there may not be a significant difference in result although both tests appear different. The latter, whilst not requiring the impermissible purpose to be the substantial purpose, nevertheless requires the impermissible purpose to be a “significantly contributing cause”. The improper purpose, if not a substantial purpose, must have triggered the impugned board action. If the improper purpose did trigger the board action and is a significant contributing cause, it is probably on some point on the spectrum that may be regarded as a substantial purpose. Thus, whichever test is used, it remains a difficult question of fact as to whether one of a number of purposes can be taken to be more important than the others in the minds of the directors.

Step 2 is concerned with the state of mind of the director or the board when they exercise the power. It is suggested that the substantial purpose test or the ‘but-for’ test may be the key to untangling the two strands of cases—those wherein the courts deferred to the director or the board and had found that they acted with a proper purpose because they acted bona fide in the interests of the company, and those wherein the courts intervened in the directors’ decision and explained that the bona fides of the director or board did not prevent them from acting improperly. It may be necessary to begin by quoting Lord Wilberforce in *Howard Smith*:<sup>35</sup>

The extreme argument on one side is that, for validity, what is required is bona fide exercise of the power in the interests of the company: that once it is found that the directors were not motivated by self-interest—i.e. by a desire to retain their control of the company or their positions on the board—the matter is concluded in their favour and that the court will not inquire into the validity of their reasons for making the issue...

On the other side, the main argument is that the purpose for which the power is conferred is to enable capital to be raised for the company, and that once it is found that the issue was not made for that purpose, invalidity follows...

It can be accepted, as one would only expect, that the majority of cases in which issues of shares are challenged in the courts are cases in which the vitiating element is the self-interest of the directors, or at least the purpose of the directors [is] to preserve their own control of the management...

Further it is correct to say that where the self-interest of the directors is involved, they will not be permitted to assert that their action was bona fide thought to be, or was, in the interest of the company; pleas to this effect have invariably been rejected...

But it does not follow from this, as the appellants assert, that the absence of any element of self-interest is enough to make an issue valid. Self-interest is only one, though no doubt the commonest, instance of improper motive: and, before one can say that a fiduciary power has been exercised for the purpose for which it was conferred, a wider investigation may have to be made.

It would appear from Lord Wilberforce’s statement above that once it is found (through applying the substantial purpose test) that the main end for which the power

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<sup>35</sup> *Supra* note 2 at 834.

is exercised is to advance self-interest, the power would have been exercised improperly. If there were evidence of self-interest, the conclusion has to be that the power was exercised improperly, regardless of how much benefit may accrue to the company from the exercise of the power in question. This has to be correct because the power is a fiduciary power and a fiduciary power must be exercised bona fide or honestly. Dixon J. in *Mills v. Mills* expressed it as such:<sup>36</sup>

Directors of a company are fiduciary agents, and a power conferred upon them cannot be exercised in order to obtain some private advantage or for any purpose foreign to the power. It is only one aspect of the general doctrine expressed by Lord Northington in *Aleyn v. Belchier*:<sup>[37]</sup> “No point is better established than that, a person having a power, must execute it bona fide for the end designed, otherwise it is corrupt and void.”

Requiring that the fiduciary power be exercised bona fide has the merit of preserving harmony with the general overarching principle that governs a fiduciary, namely, that he has a duty to act in good faith, or in reality, not to act in bad faith. ‘Good faith’ or, rather, ‘not to act in bad faith’ is a given and it sets the outer limits beyond which the director must not pass. Thus, an exercise of power not in good faith is certainly an exercise of power for an improper purpose. It is observed that the overarching principle of good faith, which sets the limits beyond which the fiduciary may not stray, is distinct from the director’s duty to act bona fide in the interests of the company. The former is concerned with ensuring that the fiduciary does not act in bad faith, whilst the latter is concerned with ensuring that the fiduciary acts in the interests of the company. As long as there is self-interest, the fiduciary would have acted for an improper purpose; this is regardless of the fact that they could have honestly believed that their act was in the interests of the company or that a benefit accrued to the company as a result of the act.

In the event that no self-interest is involved, Lord Wilberforce stated that “a wider investigation” will have to be made, although it is not entirely clear what His Lordship envisaged. It may be opportune at this moment to consider the following discussion on the distinction between the purpose of a transaction and the reason for that transaction:<sup>38</sup>

If one postulates the case of a bidder for control of a public company financing his bid from the company’s own funds—the obvious mischief at which the section<sup>[39]</sup> is aimed—the immediate purpose which it is sought to achieve is that of completing the purchase and vesting control of the company in the bidder. The reasons why that course is considered desirable may be many and varied. The company may have fallen on hard times so that a change of management is considered necessary to avert disaster. It may merely be thought, and no doubt would be thought by the purchaser and the directors whom he nominates once he has control, that the business of the company will be more profitable under his management than it was heretofore. These may be excellent reasons but they

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<sup>36</sup> (1938) 60 C.L.R. 150 at 185 (H.C.A.).

<sup>37</sup> (1758) 1 Eden. 132 at 138, 28 E.R. 634 at 637 (Ch.).

<sup>38</sup> *Brady v. Brady* [1989] 1 A.C. 755 at 779, 780 (H.L.) (Lord Oliver).

<sup>39</sup> That is, the English equivalent of s. 76 of the *Companies Act*, *supra* note 6, prohibiting the giving of financial assistance.

cannot, in my judgment, constitute a “larger purpose” of which the provision of assistance is merely an incident. The purpose and the only purpose of the financial assistance is and remains that of enabling the shares to be acquired and the financial or commercial advantages flowing from the acquisition, whilst they may form the reason for forming the purpose of providing assistance, are a by-product of it rather than an independent purpose of which the assistance can properly be considered to be an incident.

The above passage in *Brady v. Brady*<sup>40</sup> was cited with approval by the Singapore Court of Appeal in *Wu Yang Construction Group Ltd v. Mao Yong Hui*,<sup>41</sup> a case which concerned the determination of the “substantial purpose” of the board in the context of s. 76(1)(a) of the *Companies Act*, which prohibits a company from providing financial assistance to a person for the purpose of enabling them to acquire shares in the company or its holding company. It was said that the board may have many good commercial reasons for entering into a transaction, and therefore acting bona fide in the interests of the company, but if they then purposed to provide financial assistance to a person to enable them to acquire shares in the company, then s. 76(1)(a) of the *Companies Act* would be contravened, no matter that the purpose was formed with the best commercial reasons in mind.<sup>42</sup>

Taking a leaf from this “reason-purpose” analysis expounded by *Brady v. Brady*,<sup>43</sup> the duty to act bona fide in the interests of the company is relevant to the issue of what the actual purpose is. The court will ascertain the reasons for the director or board’s action because these reasons form the basis for the director or board’s purpose. It is to be expected that in many of the cases, the director or board concerned will offer reasons that they did an act because they honestly believed that it was in the interests of the company. To this end, the court takes into account the fact that the director or the board was acting bona fide in the interests of the company because the reasons help determine the purpose for the act.

Consider, for instance, *Harlowe’s Nominees*.<sup>44</sup> In that case, an issue of shares, which defeated an attempt by the plaintiff to secure control of the company by buying up its shares, was found to be a proper use of power by the board. The main purpose for the issue of shares was said to be to secure the financial stability of the company.<sup>45</sup> The main purpose was not to thwart the plaintiff’s plan to control the company although the issue of shares had that effect. Similarly, in *Teck Corporation Ltd v. Millar*, an issue of shares was held to be for a proper purpose because the main purpose of the board was to obtain the best agreement they could relating to the exploitation of mineral rights owned by the company.<sup>46</sup> The main purpose was not to defeat the plaintiff’s attempt to control the company. In *Darvall v. North Sydney Brick & Tile Co Ltd*, Mahoney J.A. expressed the view that there was a distinction between an exercise of power for the “purpose of defeating a takeover offer”, and

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<sup>40</sup> *Supra* note 38.

<sup>41</sup> [2008] 2 S.L.R.(R.) 350 at para. 48 (C.A.) [*Wu Yang*].

<sup>42</sup> *Ibid.* at paras. 58, 59.

<sup>43</sup> *Supra* note 38.

<sup>44</sup> *Supra* note 31.

<sup>45</sup> *Ibid.* at 495-497

<sup>46</sup> *Supra* note 24 at para. 156.

“one prompted by the takeover offer but, in the end, entered into because the directors bona fide believe[d] it to be in the interests of the company”.<sup>47</sup>

In the above three cases, the main purpose, whether applying the substantial purpose test or the ‘but-for’ test, was said to be that of securing a commercial advantage to the company. A decision to secure a commercial advantage is a business decision within the purview of management, hence the fact that the board was acting bona fide in the interests of the company was relevant and it was not surprising that the courts express the oft-quoted sentiment that they defer to managerial decisions. In other words, while the duty to act bona fide in the interests of the company is relevant to the ascertainment of the actual purpose in Step 2 (the duty to act bona fide in the interests of the company often providing the reasons why the director or the board acts in a particular way), the duty to act bona fide in the interests of the company cannot determine if the director or the board breaches their duty to act for proper purposes, because according to the two-step approach, the actual purpose ascertained in Step 2 has to be measured against the proper purpose earlier determined in Step 1. Thus, if the actual purpose in the above three cases was instead found to be that of depriving a shareholder of his voting majority or to defeat a takeover bid (as opposed to that of securing a business advantage for the company), the courts would have concluded that the power was improperly exercised because this actual purpose in Step 2 did not fit in with the proper purpose in Step 1, and it would not have mattered that the board bona fide believed that depriving a shareholder of his voting majority or defeating a takeover was in the interests of the company.

Although Step 2 involves a difficult question of fact as to what the actual purpose is, it is no more difficult than the trial judge having to ascertain in any litigation, say, what a director intended, knew or believed, or whether a director honestly believed what he did was in the interests of the company. Since only the director himself is in a position to give direct evidence of his subjective thought processes at a given moment, the trial judge is not at all unfamiliar with drawing inferences from what he said and did and from extraneous circumstances. Therefore, although it is difficult to determine what the substantial purpose of the director or the board is, it is a province the trial judge is well acquainted with.

#### IV. REASONS FOR THE ASCENDENCY OF THE DUTY

The duty to act for proper purposes has most frequently been applied in situations where the board is conferred a power to issue shares. Typically, when a takeover bid is about to be launched, and the board exercises the power to issue shares to, say, protect their jobs, by issuing shares to a party who is supportive of the board. Obviously, an issue of shares will upset the balance of voting power within the company, resulting in a failed takeover bid and depriving the existing shareholders who were supportive of the takeover bid a chance to exit the company. Indeed, the development of the proper purpose doctrine probably had its genesis in the context of a power to issue shares in *Fraser v. Whalley*.<sup>48</sup> The court in that case stated as *obiter dicta* that the issue of shares “for the purpose of creating votes to counteract

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<sup>47</sup> (1989) 16 N.S.W.L.R. 260 at 330 (S.C.) [emphasis added].

<sup>48</sup> (1864) 2 H. & M. 10, 71 E.R. 361 (Vice Chancellors’ Courts).

the preponderating voting power of [the bidder] and his nominees”<sup>49</sup> was for an improper purpose, and as such it would disregard the board’s bona fide belief that the bidder and his nominees would destroy the company.<sup>50</sup> Many cases<sup>51</sup> which followed were concerned with the issue of shares in which the courts applied the duty to act for proper purposes in a takeover context.

However, the duty to act for proper purposes is a flexible principle that can be applied in a wide variety of situations. In *Bishopsgate Investment Management Ltd (in liquidation) v. Maxwell (No. 2)*,<sup>52</sup> Bishopsgate Investment Management Ltd (“Bishopgate”) brought an action against Maxwell for, *inter alia*, a breach of fiduciary duty when he, exercising fiduciary powers vested in him as a director of Bishopsgate, transferred five parcels of shares for no consideration. Hoffmann L.J. (as he then was) formulated the duty to act for proper purposes in the following manner:<sup>53</sup>

Mr Maxwell was in breach of his fiduciary duty because he gave away the company’s assets for no consideration to a private family company of which he was a director. This was prima facie a use of his powers as a director for an improper purpose and in my judgment the burden was upon him to demonstrate the propriety of the transaction...

In the case of breach of the fiduciary duty, it seems to me that the cause of action is constituted not by failure to make inquiries but simply by the improper transfer of the shares to Robert Maxwell Group plc. Even if Mr Maxwell had made inquiries and received reassuring answers from other directors whom he was reasonably entitled to trust, he would not have escaped liability for a transfer which was in fact for a purpose outside the powers entrusted to the board.

Several observations may be made about Hoffmann L.J.’s statement. First, the duty applies to an individual director’s as well as a board’s exercise of powers. There is a legion of cases which are concerned with the board’s powers to issue shares,<sup>54</sup> and those decisions had to grapple with how to ascertain the *board’s* purpose<sup>55</sup> when it issued the shares. As such, there may have been a perception that the duty to act for proper purposes is applicable to an exercise of a board’s powers. *Bishopsgate Investment* has made it clear that the duty applies to an exercise of an individual director’s powers as well.

Second, Hoffmann L.J.’s formulation of the duty is very strict. It would appear from his statement that even if Maxwell had established that he had acted bona fides, that would not be relevant to the inquiry as to whether he breached the duty to act for proper purposes. It was also said in *obiter* that even if Maxwell had made inquiries, those inquiries would not have saved him if the court had determined that when he

<sup>49</sup> *Ibid.* at 22 and 366 respectively.

<sup>50</sup> *Ibid.* at 28-30 and 368, 369 respectively.

<sup>51</sup> See e.g., *Punt v. Symons & Co Ltd*, *supra* note 14, *Hogg v. Cramphorn Ltd*, *supra* note 2; *Howard Smith*, *supra* note 2.

<sup>52</sup> [1993] B.C.C. 120 (C.A.) [*Bishopsgate Investment*].

<sup>53</sup> *Ibid.* at 140.

<sup>54</sup> See e.g., *Howard Smith*, *supra* note 2; *Piercy v. S Mills & Company, Limited* [1920] 1 Ch. 77 (H.C.); *Ngurli Limited v. McCann* (1953) 90 C.L.R. 425 (H.C.A.).

<sup>55</sup> See e.g., *Harlowe’s Nominees*, *supra* note 2; *Langton v. Forsyth Mineral Exploration N.L.* (1975) 1 A.C.L.R. 227 (N.S.W.C.A.); *Hirsche v. Sims* [1894] A.C. 654 (P.C.); *Hindle v. John Cotton Ltd.* (1919) 56 Scot. L.R. 625 (H.L. (Scot.)).

signed the transfer, it was for a purpose which the court considered *objectively* to be improper.

Third, the duty to act for proper purposes is a useful supplement to various mechanisms for controlling unacceptable disposals of the company's property. These mechanisms include statutory rules imposing restraints on a company wishing to reduce its capital,<sup>56</sup> to redeem and repurchase its shares,<sup>57</sup> to provide financial assistance for the acquisition of its own shares<sup>58</sup> and to distribute dividends.<sup>59</sup> Despite the width of these provisions, they do not hinder a company's ability to give away its assets to its members in the form of directors' fees, employees' salaries or business expenses, all of which need not be paid out of profits.

In *Re Halt Garage (1964) Ltd*,<sup>60</sup> Mr. and Mrs. Charlesworth were the only directors and members of a company, and in the course of working for that company, they exercised powers conferred on them in the company's memorandum and articles to pay themselves remuneration as directors. In 1967, Mrs. Charlesworth fell ill and continued to draw remuneration, albeit at a reduced rate, although she no longer participated in the company's business. The company became unprofitable in 1968 and went into insolvent liquidation in 1971. The liquidator sought to recover sums paid to the couple on the basis that Mrs. Charlesworth had no right to be paid after she stopped work and Mr. Charlesworth was paid more than the market value of his services. The payments to Mr. Charlesworth were upheld but payments to Mrs. Charlesworth were found to be "not a genuine award of remuneration" but "a disguised gift out of capital".<sup>61</sup>

The court's approach in looking at the substance rather than the outward appearance or label the parties choose to call the transaction may also be seen in subsequent cases. In *Ridge Securities Ltd v. Inland Revenue Commissioners*,<sup>62</sup> the interest paid by the company on debentures was found to be "grotesquely out of proportion to the principal amounts secured" and thus a dressed-up distribution of the company's money.<sup>63</sup> Pennycuik J. said that:<sup>64</sup>

A company can only lawfully deal with its assets in furtherance of its objects. The incorporators may take assets out of the company by way of dividend or, with leave of the court, by way of reduction of capital, or in a winding up. They may, of course, acquire them for full consideration. They cannot take assets out of the company by way of voluntary disposition, however described, and, if they attempt to do so, the disposition is *ultra vires* the company.

The same approach may again be seen in *Aveling Barford Ltd v. Perion Ltd*.<sup>65</sup> In this case, the directors of Aveling Barford Ltd ("Aveling Barford") resolved to sell the company's property to Perion Ltd ("Perion"), a company controlled by one of the

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<sup>56</sup> *Companies Act*, *supra* note 6, Division 3A.

<sup>57</sup> *Ibid.*, s. 76(1)(b).

<sup>58</sup> *Ibid.*, s. 76(1)(a).

<sup>59</sup> *Ibid.*, s. 403.

<sup>60</sup> [1982] 3 All E.R. 1016 (Ch.).

<sup>61</sup> *Ibid.* at 1044.

<sup>62</sup> [1964] 1 W.L.R. 479 (Ch.).

<sup>63</sup> *Ibid.* at 493.

<sup>64</sup> *Ibid.*

<sup>65</sup> (1989) 5 B.C.C. 677 (Ch.) [*Aveling Barford*].

shareholders of Aveling Barford, at an undervalue. Although the transaction was not carried out when the company was insolvent, the company had no profits and was not in a position to make distributions to its members. Hoffmann J. (as he then was), stated that:<sup>66</sup>

[L]ooking at the matter *objectively*; the sale to Perion was not a genuine exercise of the company's power under its memorandum to sell its assets. It was a sale at a gross undervalue for the purpose of enabling a profit to be realised by an entity controlled and put forward by its sole beneficial shareholder. This was as much a dressed-up distribution as the payment of excessive interest in *Ridge Securities* or excessive remuneration in *Halt Garage*. The company had at the time no distributable reserves and the sale was therefore ultra vires and incapable of validation by the approval or ratification of the shareholder.

This trilogy of cases may be regarded as a supplement to the statutory rules restraining distributions and capital maintenance. Persons who wish to circumvent the statutory provisions may cause the companies to make distributions in a 'disguised' fashion. Although 'disguised' returns of capital may be caught under other statutory provisions dealing with unfair preference,<sup>67</sup> transactions at undervalue,<sup>68</sup> floating charges subject to avoidance<sup>69</sup> and fraudulent<sup>70</sup> and wrongful trading,<sup>71</sup> these statutory provisions apply when the company is insolvent or close to insolvency. Where the 'disguised' return of capital did not take place when the company is insolvent or close to insolvency, and at the same time the transaction did not fall within the scope of the statutory provisions restraining distributions and capital maintenance, recourse may have to be had to this trilogy of cases and the ruling made that the payment was 'disguised' or 'not genuine'.

Yet, going on the principle that certain distributions are 'disguised' or 'not genuine' is not without its difficulty. In *Re Halt Garage*, Mrs. Charlesworth was a member of the company, holding one out of two £1 shares. In *Aveling Barford*, Perion, the beneficiary of wrongful disposition of Aveling Barford's property was not a member of the company. It may be difficult to justify judicial intervention on the basis that the wrongful disposition or payment involved a 'disguised' return of capital to the company's members if Mrs. Charlesworth had not been a member and Perion was not actually a member. Other than the difficulty with regard to the status of the beneficiary of the wrongful distribution, 'disguise' or 'genuineness' are extremely nebulous concepts. The court will have to make an inquiry into the directors' motives, an inquiry which was eschewed by the Court of Appeal in *Rolled Steel Products (Holdings) Ltd v. British Steel Corporation*.<sup>72</sup>

The difficulty of using the principle that certain distributions are 'disguised' or 'not genuine' may also be seen in *Raffles Town Club Pte Ltd v. Lim Eng Hock Peter*.<sup>73</sup> In

<sup>66</sup> *Ibid.* at 683 [emphasis added].

<sup>67</sup> *Companies Act*, *supra* note 6, s. 329; *Bankruptcy Act* (Cap. 20, 2009 Rev. Ed. Sing.), s. 99.

<sup>68</sup> *Companies Act*, *ibid.*; *Bankruptcy Act*, *ibid.*, s. 98.

<sup>69</sup> *Companies Act*, *ibid.*, s. 330.

<sup>70</sup> *Ibid.*, s. 340.

<sup>71</sup> *Ibid.*, s. 339.

<sup>72</sup> [1986] Ch. 246 (C.A.) [*Rolled Steel Products*].

<sup>73</sup> [2013] 1 S.L.R. 374 (C.A.) [*Raffles Town Club*]. Other Singapore cases that touched on, but did not expound on, the misuse of powers to make unlawful payments or distributions include *Wu Yang*, *supra*

that case, Raffles Town Club Pte Ltd (“RTC”) sued its former directors alleging, *inter alia*, breach of director’s duties, when the former directors siphoned off funds from RTC by causing RTC to pay excessive management fees of around S\$78 million to a company known as Europa Holdings Pte Ltd (“EH”) pursuant to a sham Management Agreement (“MA”) as well as causing RTC to pay to themselves excessive directors’ fees, expenses and consultancy/incentive fees amounting to about S\$15 million.

With regard to the issue of whether the management fees were excessive, the Singapore Court of Appeal agreed with the High Court’s findings, which were that:<sup>74</sup>

[T]he court is not as well placed as commercial men such as the [former directors] to ascertain what would be the appropriate amount of remuneration for all of the work done and services provided by EH... The work done by EH in launching the Club vis-à-vis RTC is difficult to quantify with exactitude but I find that [the] 15% marketing commission is not an extortionate sum in the circumstances.

With regard to the issue of whether directors’ fees were excessive, the Court of Appeal approved *Gower and Davies’ Principles of Modern Company Law*<sup>75</sup> where it was observed that:<sup>76</sup>

The courts have been unwilling to scrutinise directors’ remuneration decisions on grounds of excess or waste, refusing even to prescribe that pay must be set by reference to market rates, provided the decision on remuneration is a genuine one and not an attempt, for example, to make distributions to shareholders/directors where there are no distributable profits.

In addition to the statutory provisions discussed earlier which were aimed at restraining unlawful distributions and distributions carried out when the company is insolvent or close to insolvency, the court had in the past made use of the *ultra vires* doctrine to allow the company to recover its assets that were wrongfully depleted. However, with the decline of the *ultra vires* doctrine, it will be the rare case where the courts will use the doctrine as a weapon to deal with the blatant misappropriation of corporate assets.<sup>77</sup>

The emasculation of the *ultra vires* doctrine in company law has done much to protect third parties dealing with the company. According to s. 23(1)(a) of the *Companies Act*, a company has full capacity to carry on or undertake any business or activity, do any act or enter into any transaction; and for the purposes of carrying out such business or activity, it has full rights, powers and privileges. Unless the company

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note 41; *Liquidators of Progen Engineering Pte Ltd v. Progen Holdings Ltd* [2010] 4 S.L.R. 1089 (C.A.); *Townsing Henry George v. Jenton Overseas Investment Pte Ltd* [2007] 2 S.L.R.(R.) 597 (C.A.); *Scintronix Corp Ltd v. Ho Kang Peng* [2013] 2 S.L.R. 633 (H.C.); *Chip Thye Enterprises Pte Ltd (in liquidation) v. Phay Gi Mo* [2004] 1 S.L.R.(R.) 434 (H.C.); *Public Prosecutor v. Lew Syn Pau* [2006] 4 S.L.R.(R.) 210 (H.C.).

<sup>74</sup> *Raffles Town Club*, *ibid.* at para. 22, citing *Raffles Town Club Pte Ltd v. Lim Eng Hock Peter* [2010] SGHC 163 at para. 137.

<sup>75</sup> Paul L. Davies, ed., *Gower and Davies’ Principles of Modern Company Law*, 8th ed. (London: Sweet & Maxwell, 2008).

<sup>76</sup> *Raffles Town Club*, *supra* note 73, citing Davies, *ibid.* at para. 14-14.

<sup>77</sup> See e.g., *International Sales & Agencies Ltd v. Marcus* [1982] 3 All E.R. 551 (Q.B.).

chooses to state its objects<sup>78</sup> or restrict its capacity or powers,<sup>79</sup> few directors or boards will be caught for making gifts that are not in furtherance of the company's objects. The *Companies Act* has ramped up protection for third parties by preventing the validity of an act done by a company from being called into question on the ground of lack of capacity.<sup>80</sup> In the past, when the *ultra vires* doctrine operated, some of the cases in which directors acted in disregard of the interests of the company were decided on the ground that the company did an *ultra vires* act. However, *Rolled Steel Products*<sup>81</sup> has drawn a firm distinction between "acts done in excess of the capacity of the company on the one hand and acts done in excess or abuse of the powers of the company on the other."<sup>82</sup>

The above developments, both in terms of statutory provisions<sup>83</sup> and judicial analyses in decisions like *Rolled Steel Products*, have contributed to the decline of the *ultra vires* doctrine, which means that a company will rarely be able to recover its assets from third party recipients who received assets from directors who misapplied those assets.

It is submitted the duty to act for proper purposes provides a test more certain and more defensible than the test of 'genuineness' and is effective, without having to resort to the *ultra vires* doctrine, in allowing the company to recover corporate assets depleted flagrantly for the benefit of insiders. When the substantial purpose of the director or the board in exercising a power to deal with the company's assets is to advance his or their own interest,<sup>84</sup> or the interest of the person whose nominee he is,<sup>85</sup> or the interest of a section of shareholders,<sup>86</sup> they would be found to have exercised their powers improperly. Egregious abuse of power can thus be curbed using the duty to act for proper purposes without having to resort to statutory provisions (rules restraining distributions and capital maintenance as well as rules which apply only when the company is insolvent) or the difficult test of 'genuineness' or the *ultra vires* doctrine. Lord Wilberforce in *Howard Smith* has made clear that an exercise of power to advance self-interest is an improper exercise of power and there would have been no need to apply the test of 'genuineness' which comes with its attendant problems.

It is also observed that the close cousin of the duty to act for proper purposes—the duty to act bona fide in the interests of the company—appears to be applied more frequently in the Singapore courts. This is so even in certain situations where it may not be felicitous to apply the duty to act bona fide in the interests of the company but it may be more apposite to apply the duty to act for proper purposes. First, the level of scrutiny as to whether the discretion is exercised bona fide in the interests of company is low. The courts do not substitute their own judgement for that of the

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<sup>78</sup> *Companies Act*, *supra* note 6, s. 23(1A).

<sup>79</sup> *Ibid.*, s. 23(1B).

<sup>80</sup> *Ibid.*, s. 25(1).

<sup>81</sup> *Supra* note 72. The case has been approved by the Singapore Court of Appeal in *Banque Bruxelles Lambert v. Puvaria Packaging Industries (Pte) Ltd (in liquidation)* [1994] 1 S.L.R.(R.) 736.

<sup>82</sup> *Ibid.* at 304 (Browne-Wilkinson L.J.).

<sup>83</sup> *Companies Act*, *supra* note 6, ss. 23, 25

<sup>84</sup> *Bishopsgate Investment*, *supra* note 52.

<sup>85</sup> *Scottish Co-operative Wholesale Society Ltd. v. Meyer* [1959] A.C. 324 (H.L. (Scot.)); *Kuwait Asia Bank E.C. v. National Mutual Life Nominees Ltd.* [1991] 1 A.C. 187 (P.C.).

<sup>86</sup> *Mills v. Mills*, *supra* note 36.

directors.<sup>87</sup> The duty to act for proper purposes, on the other hand, provides the court greater leeway to intervene in the directors' decision-making because it envisages an objective test. Ascertaining what the 'proper purposes' are, for the exercise of a power, is a matter of law for the court to decide.

Second, the issue of whose interests are regarded as the company's interests has not been settled. It is unclear if the directors should consider the interests of the company as an entity, or its members or its employees or its creditors, or in the case of a company in a corporate group, the interests of the group. An associated question is how the directors should balance considerations in favour of a short-term perspective against a long-term view. For instance, when the company is the target of a takeover bid which promises favourable terms for shareholders who wish to sell, should the directors consider transactions which could in the long-term bring greater benefits to shareholders than they would receive by acceptance of the offers? If there is no clarity as to what the interests of the company are, it would be difficult to conclude whether a director or board's decision is in the interests of the company.

The duty to act bona fide in the interests of the company, though applied far more often than the duty to act for proper purposes, appears no less easy to apply than the duty to act for proper purposes, and may in some instances, allow directors to escape liability even if they have positively harmed the company.<sup>88</sup>

## V. CONCLUSION

It would appear that the court looks objectively at the purposes for which a particular power was conferred and then determines whether on the evidence the directors used the power for a permissible purpose, irrespective of whether they were acting in good faith. The bona fides of a director is not in and of itself the yardstick of the propriety of a director's action. Thus the duty to act for proper purposes is not a proxy for assessing bona fides, but is instead concerned with whether a particular power conferred for specific purposes has been exercised for the correct and intended ends.

It would appear that the duty to act for proper purposes occupies a position in between the subjective and objective tests. While Step 1 involves an objective categorisation as to what are proper purposes, Step 2 involves the court making a finding of fact as to whether one of a number of purposes can be taken to be more important than others in the minds of the directors, based on inferences from what the director said or did or from extraneous circumstances, in order to determine the director's subjective thought processes at a given moment. Step 2, therefore, takes into account the duty to act bona fide in the interests of the company in that the duty is also concerned with the intentions of the director rather than the objective qualities of the action. It is submitted that the proper purpose doctrine is an ingenious attempt to marry the directors' belief and the law's belief in a single tool to review the directors' decisions.

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<sup>87</sup> *Re Smith and Fawcett, Limited*, *supra* note 1. It may be seen in many Singapore cases, e.g., *ECRC Land Pte Ltd (in liquidation) v. Ho Wing On Christopher* [2004] 1 S.L.R.(R.) 105 (H.C.); *Vita Health Laboratories Pte Ltd v. Pang Seng Meng* [2004] 4 S.L.R.(R.) 162 (H.C.).

<sup>88</sup> *Tokuhon (Pte) Ltd v. Seow Kang Hong* [2003] 4 S.L.R.(R.) 414 (C.A.).

The duty to act for proper purposes may be applied in many situations and is expressed in very general terms. Because it is expressed as a general principle, it is an extremely flexible tool which is capable of use in dynamic and diverse situations. It is hoped that the Singapore courts will have occasions to consider the duty to act for proper purposes and hence develop the duty as an important tool to review the directors' decisions.