

DIRECTOR'S DUTIES: RE-EXAMINING THE BONA FIDE TEST

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I. INTRODUCTION

It is well-established that directors are fiduciaries of the company they serve. As fiduciaries, they owe a host of duties, including the duty to act bona fide in the company's best interests. Unfortunately, recent developments have created uncertainty over how the test is to be applied. In particular, whether the test has a substantive objective component in addition to a subjective one. The dominant interpretation is that both components are part of the test. However, closer inspection exposes some flaws in this interpretation. This article will explore the arguments for the contrary position: that the test for the duty to act bona fide in the company's interests is purely subjective.

II. THE ORIGINAL TEST

Originally, the Singapore courts' test for assessing bona fides was purely subjective. Directors need only act in "what they consider – not what a court may consider – is in the interests of the company" to satisfy the duty.¹ Courts were motivated by "strong policy considerations" to avoid "coerc[ing directors] into exercising defensive commercial judgment" that "will dampen, if not stifle, the appetite for commercial risk and entrepreneurship".² As such, the duty would not be breached if the directors acted in the "honest and reasonable belief that they were for the best interest of the company, even if those decisions turned out subsequently to be money-losing ones".³

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¹ *Cheong Kim Hock v Lin Securities* [1992] 2 SLR 349 [*Cheong Kim Hock*] at para 26.

² *Vita Health Laboratories Pte Ltd v Pang Seng Meng* [2004] 4 SLR 162 [*Vita*] at para 17.

³ *ECRC Land Pte Ltd v Ho Wing On Christopher* [2004] 1 SLR(R) 105 at para 49.

It is apposite to note that the test may occasionally dip into the realm of objectivity. This is also known as the evidential standard version of the objective test. In the Singapore High Court case of *Cheam Tat Pang v PP*⁴ the Learned Judge made the following remark:⁵

“It is settled law that if directors take risks which no director could honestly believe to be taken in the interests of the company, such actions could well support allegations that the directors in question had acted in breach of their fiduciary duties to the company”.

The Learned Judge’s remarks appear limited to establishing the evidential proof of the subjective mind of the director in question to see if he did in fact act reasonably. As such, the evidential objectivity did not detract from the overall subjectivity of the test.

III. THE DOMINANT INTERPRETATION OF THE CURRENT TEST

The locus classicus for the new test is *Ho Kang Peng v Scintronix*.⁶ The facts of the case are simple: the defendant director effectively paid bribes to advance the company’s overseas interests.⁷ In applying the bona fide test, the courts stated:⁸

“However, this does not mean that the court should refrain from exercising any supervision over directors as long as they claim to be genuinely acting to promote the company’s interests. First, “where the transaction is not objectively in the company’s interests, a judge may very well draw an inference that the directors were not acting honestly”... The test in *Charterbridge Corporation Ltd v Lloyds Bank Ltd* [1970] Ch 62 (at 74) of “whether an

⁴ [1996] 1 SLR 541.

⁵ *Ibid* at para 80.

⁶ [2014] 3 SLR 0329 [*Scintronix*].

⁷ *Ibid* at paras 32-34.

⁸ *Ibid* at paras 38-39.

intelligent and honest man in the position of a director of the company concerned, could, in the whole of the existing circumstances, have reasonably believed that the transactions were for the benefit of the company”, has been accepted and applied by this court in *Intraco (CA)* (at [28]). On the other hand, it will be difficult to find that a director has acted bona fide in the interests of the company if he “take[s] risks which no director could honestly believe to be taken in the interests of the company”... Secondly, it seems that the requirement of bona fide or honesty will not be satisfied if the director acted dishonestly even if for the purported aim of maximising profits for the company.” (emphasis added)

By advocating for the standard of an “intelligent and honest man”, and stating that acting for the company’s best interests would be insufficient, the courts seemed to be introducing a substantive objective component.

This interpretation of *Scintronix* has been largely accepted as the orthodoxy. Subsequent cases, such as the Singapore Court of Appeal case of *Goh Chan Peng v Beyonics Technology Ltd*⁹ appear to support this view, stating that the bona fide test has “both subjective and objective elements”.¹⁰ Eminent local academics such as Professors Dan Puchniak and Tan Cheng Han SC have also adopted the position that the test has a substantive objective component.¹¹

⁹ [2017] 2 SLR 592 [*Beyonics*].

¹⁰ *Ibid* at para 35.

¹¹ D Puchniak, CH Tan & SS Tang, “Company Law” (2017) 18 SAL Ann Rev 247 at paras 9.7-9.8.

IV. THE ALTERNATIVE INTERPRETATION OF THE CURRENT TEST

A. *Case Authority supporting a Purely Subjective Standard*

A closer inspection of *Scintronix* reveals that it may not have laid down a discrete objective component at all. Phrases like “intelligent and honest man” which hinted at an objective standard were tempered with statements that they would only be used to “draw an inference” or when directors only “purport” to act in the company’s best interest.¹² This suggests that the courts were only advocating the use of an objective evidentiary tool to determine the director’s subjective state of mind, keeping in line with the traditional test. Furthermore, the court never explicitly stated that there would be an objective component. This is an odd oversight considering the uninterrupted pedigree of the purely subjective test.

The apparent support of *Beyonics* is also to be doubted. The court commented that “where the transaction is not objectively in the company’s interests, a judge may very well draw an inference that the directors were not acting honestly” (emphasis added).¹³ This statement suggests that the courts were using an objective evidentiary tool as explicated by Professor Walter Woon. This possibility was noted by the Singapore High Court in *Ong Bee Chew v Ong Shu Lin*,¹⁴ acknowledging that *Beyonics* could have merely used an objective evidentiary tool. We note that while *Ong Bee Chew* did ultimately support the two-part test, this was for procedural fairness rather than doctrinal accuracy as *Beyonics* was not available to the parties at the time of their submission.¹⁵

¹² *Scintronix*, *supra* note 6 at paras 32-34.

¹³ *Beyonics*, *supra* note 9 at para 36.

¹⁴ [2017] SGHC 285 [*Ong Bee Chew*] at para 78.

¹⁵ *Ibid* at para 78.

Furthermore, as suggested by Professor Hans Tjio, *Scintronix* may have simply applied the original *Charterbridge* test instead.¹⁶ The court in *Charterbridge Corporation Ltd v Lloyds Bank Ltd*¹⁷ held that the objective standard of an “an intelligent and honest man” would only be applied where the director exercised no discretion at all.¹⁸ The rationale behind it is simple – failing to engage in any subjective consideration whatsoever, an objective assessment remained the only way to determine if he had acted in the company’s interests.¹⁹ In *Scintronix*, the court found that “[t]he wrong committed by the Appellant in the present case cannot be regarded as an error of judgment – it arose because he failed to exercise any judgment at all.” (emphasis added).²⁰ As determined by Professor Tjio, this indicates *Scintronix* was merely a use of the original *Charterbridge* test in Singapore, applying the objective standard only when no discretion was exercised.²¹ This would leave the traditional subjective test largely intact.

B. Policy Arguments supporting a Purely Subjective Standard

The main public policy rationale for a substantive objective component is to prevent directors from carrying out immoral acts they believe were in the company’s best interests. Under a purely subjective test, he would be exonerated, lowering the standards of commercial morality. However, the need to maintain a minimum standard of commercial morality must be balanced against the need to avoid stifling entrepreneurship with excessive judicial interference.

Unfortunately, the two-part test risks stifling entrepreneurship. Its vagueness instils undue fear in directors who would be unsure of what standard to act on. Courts have elucidated that the objective

¹⁶ Hans Tjio, P Koh & PW Lee, *Corporate Law* (Academy Publishing, 2015) [Tjio, Koh & Lee (2015)] at para 09.043.

¹⁷ [1970] Ch 62 [*Charterbridge*].

¹⁸ *Ibid* at 74.

¹⁹ Tjio, Koh & Lee (2015) *supra* note 16 at para 09.043.

²⁰ *Scintronix*, *supra* note 6 at para 40.

²¹ Tjio, Koh & Lee (2015) *supra* note 16 at para 09.043.

component depends on whether, “objectively, the transactions were not in the company’s interests”.²² However, in an attempt to mitigate judicial interference, they have softened the standard, stating that is only serves to “[hold] directors to minimum standards of commercial morality” and that the court will thus apply “a very low baseline in order to avoid unnecessary interference”.²³ Unfortunately, ‘commercial morality’ is a nebulously defined criterion that does little to resolve the uncertainty.

Furthermore, the test is phrased very widely as it takes the perspective of an ‘honest and intelligent director’ such that even negligence can potentially fall under the objective limb. This problem was evident in *Scintronix* where the court made the following remark:²⁴

“He simply continued a highly irregular and improper practice which he understood to have been initiated by the previous management under a different form without so much as inquiring why it was made, whether it would implicate the Company, and whether proper sanction had been obtained. *He had failed to exercise reasonable care.*”
(emphasis added)

While the subsequent cases of *Beyonics* and *Ong Bee Chew* all stressed a ‘minimum standard’, they never repudiated *Scintronix*’s requirement for ‘reasonable care’ such that it is possible for the broad standard to persist since that would comport with what is expected of an ‘honest and intelligent’ director.

If the objective standard is truly, as a plain reading of the judgement indicates, that of an ‘honest and intelligent director’, the substantive objective test would impose too harsh a burden on directors. This is as 99% of all domestic companies are Small Medium Enterprises.²⁵ It is unrealistic to expect

²² *Beyonics*, *supra* note 9 at para 35.

²³ *Ong Bee Chew*, *supra* note 14 at para 84.

²⁴ *Scintronix*, *supra* note 6 at para 40.

²⁵ Singapore Department of Statistics, “Topline Estimates For All Enterprises And SMEs, Annual” (accessed 2 January 2021)

small businesses to have the funds to hire professionals to function as directors. Nor is it realistic to expect all business owners, many of whom are uneducated, to perform the role of an “honest and intelligent director”. Imposing such an exacting standard would “dampen, if not stifle, the appetite for commercial risk and entrepreneurship”.²⁶

C. *Applying the Purely Subjective Test to existing Case Law*

The existing case law has dealt solely with the issue of bribery. Bribery satisfies the targeted fact matrix of being both immoral and *prima facie* in the company’s interest. However, such situations could have been easily prevented by a purely subjective test. As noted in *Scintronix*, bribery does not help the company’s long-term interests, only its short-term interests.²⁷ Ergo, a director could subjectively believe giving a bribe to be in the company’s short-term interest but still fail to subjectively believe it is in the company’s interests as a whole, after taking its long-term interests into account. The situation of receiving a bribe, as in *Beyonics*, is much more straightforward – the director accepted a bribe to do something he otherwise would not have done. It is unlikely any director could subjectively believe that accepting a bribe would further the company’s interests.

V. CONCLUSION

The bona fide test plays a critical role in regulating director’s duties. Uncertainty over its components could prompt unwarranted defensive decision making, curtailing the economic potential of Singapore’s businesses. A clearer test is therefore needed. While we hope that the courts will take the flaws of the two-part test into account, we recognise that the current orthodox interpretation of the bona fide test will likely remain the law for the foreseeable future. Our article merely aims to explore the possibility of an alternative rather than to overturn the status quo.

<<https://www.tablebuilder.singstat.gov.sg/publicfacing/createDataTable.action?refId=15808>>

²⁶ *Vita*, *supra* note 2 at para 17.

²⁷ *Scintronix*, *supra* note 6 at para 37.