

LEGISLATION UPDATE

29 October 2014

AMENDMENTS TO THE COMPANIES ACT – POWER OF DIRECTORS TO BIND COMPANIES

INTRODUCTION

This article is the second in a series of legal updates relating to the amendments to the Singapore Companies Act (“**Companies Act**”) to be effected by the Companies (Amendment) Bill No. 25 of 2014 (“**Amendment Bill**”).

Many of the amendments in the Amendment Bill are expected to come into force by the end of 2014, and this Legal Update highlights and discusses the amendments relating to the power of directors to bind a company.

New section 25B

The amendments in the Amendment Bill (the “**Amendments**”) introduce a new section 25B which provides that a third party dealing with a company in good faith need not concern itself with whether the directors of the company are in breach of any limitations in the company’s constitution. In this regard, aside from limitations contained in the company’s constitution itself, this would include any limitations deriving:

- (a) from a resolution of the company or any class of shareholders; or
- (b) from any agreement between the members of the company or of any class of shareholders.

To some degree, this extends the “indoor management rule” under common law, which effectively states that a person dealing with a company may assume that any internal procedures contained in the company’s constitution had been properly complied with.

This new section is intended to protect third parties dealing with the company from any internal restrictions that may be contained in the company’s constitution which limits the power of the board to act on the company’s behalf, provided that the third party has acted in good faith. For example, where a company’s constitution contains a provision which requires the unanimous consent of the board for contracts over a certain value, and a contract of that nature was entered into without unanimous consent having been obtained, the counterparty should still be allowed to enforce the contract so long as he was dealing with the company in good faith.

Further pursuant to the new section 25B(2), a person dealing with a company:

- (a) is not bound to enquire as to any limitation on the powers of the directors to bind the company or authorise others to do so; and
- (b) is presumed to have acted in good faith unless the contrary is proved.

While it is stated that a person is “not bound to enquire” whether there are limitations on the directors’ powers, English courts have indicated that the UK equivalent of this provision does not absolve a person dealing with a company from having to enquire whether the persons acting for a company are authorised where the circumstances are such as to put that person on enquiry. Accordingly, if there are suspicious circumstances or abnormal transactions, there may be an expectation that the third party dealing with the company is put on notice and therefore ought to make reasonable enquires.

What is “good faith”?

With respect to the meaning of “good faith” and how a lack of “good faith” is established, the new section 25B(2) differs slightly from its UK

equivalent¹ in that the UK provision explicitly provides that a person shall not be regarded as acting in bad faith by reason only of his knowing that an act is beyond the powers of the directors under the constitution. It therefore remains to be seen if the Singapore courts will find that knowledge of an act which is beyond the powers of the directors will, by itself, be sufficient to establish lack of good faith for the purposes of the new section 25B(1).

Limitation on transactions entered into by directors or persons connected with directors

Section 25B will be subject to the new section 25C that is intended to prevent directors of a company from taking advantage of any purported corporate acts in excess of their powers. In gist, where any transaction is entered into by a company with its directors or a director of the company's holding company, or a person connected with any such director, section 25C provides that such a transaction may, notwithstanding section 25B, still be voidable at the instance of the company if it was entered into without authority.

Further under section 25C(4), such directors and/or connected persons mentioned above and any director of the company who authorised the transaction are also liable to account to the company for any gain they have made directly or indirectly by the transaction, and to indemnify the company for any loss or damage resulting from the transaction.

Persons who may be considered connected to a director for the purposes of section 25C include a member of the director's family, a company in which the director is interested in at least 20% of the share capital, and a person acting in his capacity as trustee of a trust the beneficiaries of which include the director or any member of his family.

Section 25C(6) also provides that any person, other than a director of the company concerned, who as a consequence of section 25C(4) may be liable to account for gain to the company, or to indemnify it against loss or damage, will have a defence to those liabilities if he can show that at the time the transaction in question was entered

into, he did not know that the directors were exceeding any limitations on their powers in causing the company to enter into the transaction.

Under section 25C(5), the transaction will also cease to be voidable if:

- (a) restitution of the asset is impossible;
- (b) the company has been indemnified against any loss or damage suffered by it;
- (c) rights acquired by a *bona fide* purchaser for value without actual notice of the contravention and who is not a party to the transaction would be affected if the transaction were voided; or
- (d) the company has affirmed the transaction.

CONCLUSION

The new sections 25B, 25C and 25D to be introduced by the Amendments to the Companies Act will have some impact on a director's power to bind his company. While the Amendments are generally protective of third parties, parties contracting with a company may need to demonstrate that they have acted in good faith (eg by making reasonable enquiries as to whether the directors have been authorised to enter into the transaction on behalf of the company) if there are abnormal or unusual circumstances warranting it.

REFERENCES

Please also refer to the other article below which forms part of a series of legal updates relating to the Amendment Bill:

Amendments to the Companies Act – Impact on Corporate Transactions

¹ Section 40(2)(b) of the UK Companies Act 2006

If you have any questions or comments on this article, please contact:



Sean Ng
Director, Corporate & Finance
T: +65 6531 2724
E: sean.ng@drewnapier.com



Lam Shiao Ning
Director, Corporate & Finance
T: +65 6531 2278
E: shiaoning.lam@drewnapier.com

The content of this article does not constitute legal advice and should not be relied on as such. Specific advice should be sought about your specific circumstances. Copyright in this publication is owned by Drew & Napier LLC. This publication may not be reproduced or transmitted in any form or by any means, in whole or in part, without prior written approval.

Drew & Napier LLC
10 Collyer Quay
#10-01 Ocean Financial Centre
Singapore 049315

www.drewnapier.com

T : +65 6535 0733
T : +65 9726 0573 (After Hours)
F : +65 6535 4906