DREW & NAPIER

LEGAL UPDATE

CASE UPDATE

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STATUTORY DERIVATIVE ACTION IS NOT AVAILABLE ONCE A COMPANY IS IN LIQUIDATION

***Petroships Investment Pte Ltd v Wealthplus Pte Ltd and others and another matter* [2016] SGCA 17**

INTRODUCTION

In the recent case of *Petroships Investment Pte Ltd v Wealthplus Pte Ltd and others and another matter* [2016] SGCA 17, the Court of Appeal held that a statutory derivative action under s 216A of the Companies Act is not available once a company is in liquidation.

This is the first time the issue has been considered in Singapore, and the court approached the question on the basis of first principles, through a review of the statutory text, legislative history and foreign case law.

BACKGROUND

The appellant, Petroships Investment Pte Ltd ("**Petroships**"), was a minority shareholder of Wealthplus Pte Ltd ("**Wealthplus**") with a 10% shareholding.

Disagreements among the directors led to a series of successive suits that Petroships commenced against Wealthplus, amongst others, from 2009 to 2011. All were struck out.

On 19 June 2012, Petroships served notice on Wealthplus' directors as required under s 216A(3)(a) of the Companies Act. The notice stated Petroships' intention to apply for leave to bring a statutory derivative action in Wealthplus' name against its directors if they failed to provide, within 14 days, a full explanation of four transactions that Wealthplus had entered into, or to commence legal actions against the directors for having made those transactions and seek the recovery of the transferred monies. Petroships had alleged that the transactions were not in Wealthplus' interests.

Wealthplus' directors did not act on Petroships' notice. On 14 August 2012, Petroships filed Originating Summons No 766 of 2012 ("**OS 766**") to seek the court's leave to commence a derivative action against two groups of defendants. The first group comprised Wealthplus' directors and the second group comprised Wealthplus' majority shareholders and their ultimate holding company. The subject matter of the proposed derivative action was the four transactions.

On 21 August 2012, one week after OS 766 was filed, Wealthplus was placed in members' voluntary liquidation through a special resolution passed by the requisite majority of its shareholders.

DECISION OF THE HIGH COURT

The High Court judge dismissed Petroships' application for leave on two grounds.

First, the requirement of good faith under s 216A(3)(b) was not met.

Second, the requirement under s 216A(3)(c) was also not met as the derivative action was not prima facie in the interests of Wealthplus.

The judge considered that in liquidation, control shifted from the majority shareholders to the liquidator. It was the liquidator, not the board of directors, who was empowered under the Companies Act to bring or defend legal proceedings in the name of the company. Hence, the underlying rationale for a derivative action "largely" disappeared.

Petroships appealed.

Decision of the Court of Appeal

The Court of Appeal held that the threshold issue was whether s 216A was even applicable in the first place, as Wealthplus was already in liquidation. The High Court's approach in assessing whether the pre-requisites in s 216A were fulfilled was to "put the cart before the horse".

The Court of Appeal observed that there was no directly relevant case law that could provide an answer. Hence, it approached the question on first principles through a review of the statutory text, the legislative history of s 216A and case law, and made the following observations.

(a) Statutory text

The text of s 216A suggests that it was intended to apply in a situation where the directors are in active management. For instance, s 216A(3)(a) stipulates that no action may be brought unless that the complainant has given the directors of the company 14 days' notice of its intention to apply for leave to commence the action if the directors do not bring, diligently prosecute or defend or discontinue the action.

However, in liquidation, the liquidator takes over management duties. The directors effectively have no power to react to any notice served pursuant to s 216A(3)(a), whether to prosecute, defend or discontinue an action on the company's behalf.

(b) Legislative history

The legislative history of s 216A supports this interpretation.

S 216A of the Singapore Companies Act was based on legislation in Canada. For instance, like Singapore's s 216A, the notice pre-requisite in Canadian legislation requires complainants to give the directors notice of their intention to apply for leave to commence derivative action.

The Court of Appeal in this case examined Canadian legislation and law committee reports extensively, and found no indication that s 216A was intended to be available as a shareholder's remedy in the context of a company that has been placed in liquidation.

(c) Case law

As observed earlier, there is no directly relevant case law on s 216A in Singapore. Hence, the Court of Appeal turned to English, New Zealand and Australian case law.

While the statutes in these jurisdictions are worded differently from s 216A, the Court of Appeal found the reasoning in the foreign cases useful in interpreting s 216A of the Singapore Companies Act in so far as the rationale for statutory derivative action was the same.

As an aside, the Court of Appeal clarified that because s 216A is only available to Singapore private companies and public-listed companies, the common law derivative action must necessarily remain for foreign companies.

However, the court declined to make a holding on whether a shareholder who can avail himself of s 216A can nevertheless choose to rely on the common law derivative action.

In any event, a common law derivative action would not be available once a company is in liquidation.

Accordingly, the Court of Appeal dismissed Petroships' appeal. It held that s 216A does not avail a minority shareholder in the situation when the company is in liquidation, as Wealthplus was in this case. This includes a situation where the winding up is voluntary.

Comments

The Court of Appeal has provided useful clarification on this novel issue. In particular, when a company enters into liquidation, the duties and powers of management are exercised by the liquidator rather than the directors. It would be up to the liquidator to commence corporate actions. Hence, a derivative action is not available to shareholders.

Nonetheless, aggrieved shareholders of a company in liquidation are not left without remedies.

As the Court of Appeal alluded to in this case, once a company is in liquidation, the proper cause of action for minority shareholders is likely to be against the liquidator rather than a derivative action against the company directors.

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