7. COMPANY LAW

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Lifting the corporate veil

7.1 *New Line Productions, Inc v Aglow Video Pte Ltd* [2005] 3 SLR 660 ("*New Line Productions, Inc*") was a consolidated hearing of several suits involving copyright infringement of three cinematograph films had been consolidated. There were a number of defendants, including Aglow Video Pte Ltd ("Aglow"), which was a company engaged in the business of importing and distributing wholesale cinematograph films in various video formats, including video home system ("VHS"), digital versatile disc ("DVD") and video compact disc ("VCD"). Other defendants included TS Laser Pte Ltd ("TS Laser") and TS Entertainment Pte Ltd ("TS Entertainment"), both of whom carried on business in conjunction with a number of other companies and business entities under the name and style "TS Group", and were involved in the retail of films in video format. The TS Group was one of the largest video retail chains in Singapore. Other companies within the TS Group, as well as directors and officers of such companies, were also made defendants.

7.2 In June 2003, Aglow imported 3,000 copies of a film titled "Lord of the Rings – The Two Towers" ("TTT") in VCD format into Singapore, and distributed them through the TS Group outlets. The plaintiffs then commenced Suit No 718 of 2003, and obtained an interim injunction on 11 July 2003 prohibiting the defendants in that action from dealing with the infringing TTT VCDs and ordering delivery-up of the remaining ones. The defendants eventually delivered up six copies of TTT. However, the TS Group outlets, save for the one at Suntec City, which was operated by TS Entertainment, continued to sell TTT. It was only then that the plaintiffs realised that each outlet was operated by a different company, with all the companies allegedly independent from one another, and maintaining their own accounts. TS Entertainment operated only the Suntec City outlet.

7.3 The plaintiffs then issued letters of demand to all the companies in the TS Group. However, these companies refused to abide by the terms of the injunction obtained earlier by the plaintiffs. Instead, they proceeded to obtain further supplies of another 7,000 TTT VCDs through Speedy Video

Distributors Pte Ltd ("Speedy Video"). Accordingly, the plaintiffs commenced action against these companies as well, in Suit No 843 of 2003. Around that time, Suit No 836 of 2003 was also commenced against Aglow and its officers in respect of two other films, and an injunction was obtained against them pursuant to that action.

7.4 The three actions mentioned above were consolidated and tried together, with the plaintiffs seeking an injunction and damages, or in the alternative, an account of profits for infringement of copyright in the three films in issue. They also sought to lift the corporate veil in order to make the directors and officers of the companies involved personally liable for the infringement.

7.5 Tay Yong Kwang J found that Aglow and the TS Group had knowingly breached the plaintiffs' copyright. Accordingly, their defence, which was based upon their being innocent retailers dealing with what they believed to be genuine parallel imports, failed.

7.6 His Honour went on to hold that, far from being a loosely-knit group, the companies in the TS Group were really little pieces of mosaic forming a complete mural, glued together by the four directing minds behind the group, who were the common directors, officers and shareholders of the companies within the group. The business cards of these four persons intimated that TS Laser was the parent, or nerve centre, and that all the listed outlets were merely its offspring. In two newspaper articles, one of the four individuals constituting the directing minds, one Joseph Toh ("Toh"), was described as the group marketing manager for the TS Group. In his affidavit of evidence-in-chief, he described himself as a sales manager, without specifying the company which employed him. The group also had a privilege card scheme applicable to all the outlets. All the outlets bore the initials "TS", a trademark owned by TS Video Centre Pte Ltd. The plastic carrier bag used by them listed the chain of outlets. The companies in the group also shared many common directors and shareholders, and took instructions from one Clement Lau ("Lau"), who appeared to be the beneficial owner of practically all of the companies. The headquarters of the group was in Lam Leong Building in Geylang Lorong 17, which also served as the warehouse, and was owned by several of the companies in the group.

7.7 In the circumstances, Tay J felt (see [99]) that it would be entirely just to lift the corporate veil, and regard the companies for what they all really were, *ie*, the business vehicles of Lau and his family. On this footing, the court's findings should therefore apply to all the companies in the group.

Since the VCDs of TTT were infringing products, the entire TS Group was liable for having dealt with the products.

7.8 His Honour also held that the four individuals who were the "directing minds" were personally liable for the copyright infringements of the companies within the TS Group. He held, further, that one of the directors of Aglow was personally liable for Aglow's infringing acts. While Tay J accepted the general rule that officers of a company were not liable for the tortious acts committed by the company, he held that an exception arose where directors ordered an act by the company which amounted to a tort by the company. In such cases, these officers could be liable as joint tortfeasors, on the basis that they had "procured or directed" the wrong to be done. His Honour found that this was indeed the case for the four directing minds of the TS Group, as well as for one of the directors of Aglow.

7.9 *New Line Productions, Inc* illustrates very nicely how the courts may be more willing to lift the corporate veil where corporate vehicles have been used for dishonest purposes. It has been argued elsewhere by this author that at the heart of the cases where the corporate veil has been lifted, the courts have felt that the corporate form has been abused to further an improper purpose, and not for a *bona fide* commercial transaction: see Tan Cheng Han, "Piercing the Separate Personality of the Company: A Matter of Policy?" [1999] Sing JLS 531. Certainly, based on the findings of Tay J, there can be little doubt that using corporate vehicles to infringe copyrights belonging to others is an abuse of the privilege of incorporation. Such cases provide the most obvious examples of when the general rule of separate personality may be departed from.

Corporate governance

7.10 In *Jumabhoy Rafiq v Scotts Investments (Singapore) Pte Ltd* [2005] 1 SLR 45 the issue of directors' remuneration fell to be decided. The plaintiff, who was a director of the defendant company at the material time, sought remuneration on a time-costs basis or, alternatively, on a *quantum meruit* basis.

7.11 The Court of Appeal dismissed the claim. First, it was held that when the defendant company passed resolutions to empower the plaintiff to carry out certain acts on behalf of the company, resolving to "indemnify" him for all "costs and expenses" that he incurred, this did not, as a matter of interpretation, constitute an agreement to remunerate him for what he subsequently did. The court felt fortified in this view by the fact that the

company's articles would be inconsistent with the argument being advanced by the plaintiff. Under the articles, the rate of remuneration to be paid to a director, other than the managing director, had to be approved by the shareholders in general meeting. Alternatively, if a director was performing extra services to the company, the board could remunerate the director by the payment of a fixed sum. In the present case, the shareholders had not approved the rate of remuneration, nor was the plaintiff claiming a fixed sum.

7.12 The plaintiff's claim for a *quantum meruit* payment also failed, on the grounds that such a payment to directors had to be in accordance with the articles. The court went on, however, to consider whether any equitable allowance should be allowed. Assuming that there was such a jurisdiction for the court to grant an equitable allowance to a company director, the Court of Appeal held that the plaintiff had not shown why such an allowance should be paid to him. His claim for time-costs would put him in a position of conflict with the interests of the company, as the slower he worked, the more he would benefit from the arrangement at the expense of the company. The Court of Appeal emphasised part of Lord Goff of Chieveley's judgment in *Guinness Plc v Saunders* [1990] 2 AC 663 at 700–701, where Lord Goff had said, at 701, that any equitable allowance should only be provided in those cases "where it cannot have the effect of encouraging trustees, in any way, to put themselves in a position where their interests conflict with their duties as trustees".

7.13 In another case, *Pacrim Investments Pte Ltd v Tan Mui Keow Claire* [2005] 1 SLR 141 ("*Pacrim*"), the plaintiff had sought to register transfers of shares of the company. The first defendant, who was the company secretary of the company, had declined to register the share transfers on the grounds that the purported transfer had to be referred to the Official Assignee because the transferor was a bankrupt. As regards the claim against the company secretary, Andrew Ang JC (as he then was) opined that the secretary of a company was its administrative officer. The secretary ensured that the company complied with the many regulatory provisions governing the company; these included functions such as the keeping of registers, service of notices of meetings, the taking of minutes, and the filing of prescribed forms. It was his function to carry out or implement decisions of the board of directors, but he had no power to participate in the management of the company's affairs. Accordingly, he could not negotiate or conclude contracts on the company's behalf, save on the instructions of the board given in connection with the administration of the company's organisation. Nor could he register transfers of shares without the board's

authority. In his Honour's view, therefore, the company secretary had wrongly been made a defendant to the action.

Shares

7.14 Another issue that was raised in *Pacrim* (*supra* para 7.13) involved share registration. In that case, Ang JC held that the effect of s 121 of the Companies Act (Cap 50, 1994 Rev Ed) ("the Act") was not to limit the grounds upon which a company might refuse registration to those grounds set out in the articles only. Rather, the section conferred on a transferee the right to call for registration (under the articles of association), where previously such a right would have been enjoyed only by members. This is an interesting development because it might have been thought (as Ang JC himself had initially thought) that the articles of association pursuant to s 39(1) of the Act only constituted an agreement between the members *inter se* and between the members and the company, and that a transferee who was not yet a member of the company could not acquire any rights under the articles of association.

7.15 Perhaps an alternative approach that would achieve the same effect is to say that a transferee of shares acquires a presumptive right to have such shares registered, by virtue of the transferee's beneficial ownership of the said shares. However, the right to register is not absolute; there may be good reasons for the directors to refuse registration, whether those reasons arise out of the articles, or for some other good reason, *eg*, pursuant to an agreement outside the articles to restrict the transfer of the shares. Whatever the basis of the decision in *Pacrim*, the result of that case was that the court upheld a moratorium against transfer, holding that the company in question was entitled to refuse registration.

Minority oppression

7.16 In *Hoban Steven Maurice Dixon v Scanlon Graeme John* [2005] 2 SLR 632, the first plaintiff was the managing director of the third defendant ("the Company"). The second plaintiff was a company founded by the first plaintiff for the purpose of holding shares in the Company. The first and second defendants were the directors and shareholders of the Company. The plaintiffs claimed against the first and second defendants on the basis of minority oppression under s 216 of the Act. It was alleged that the first and second defendants had systematically disregarded the plaintiffs' rights. This allegation was denied by the defendants.

7.17 Prior to the actual commencement of the hearing, the parties agreed that the court need no longer determine the issue of liability. The sole issue that remained was the pricing mechanism for the sale and purchase of the second plaintiff's shares in the Company. An accountant was eventually appointed to value the shares. The plaintiffs were dissatisfied with his valuation, and invited the court to make an express finding establishing oppressive conduct on the part of the first and second defendants, thereby entailing relief pursuant to s 216. It was suggested, in the alternative, that even in the absence of any finding of oppression, the court was still empowered to exercise the powers conferred on it by s 216. A further argument was made that the Company should, on equitable grounds, be wound up.

7.18 V K Rajah J stated that it was amply clear from the provisions of s 216(2) that the power of the court to grant relief was predicated upon the court being of the opinion that the relevant grounds for granting relief set out in s 216(1) had been established (see [12]). It was therefore axiomatic that the court could not exercise, or assume, any jurisdiction to grant relief pursuant to s 216(2), unless the petitioner had established a case of oppression and/or discriminatory and/or prejudicial conduct.

7.19 In the proceedings in question, the parties had, at the outset, resolved to set aside their grievances on liability and blameworthiness, in an attempt to narrow down their differences: see [17]. In fact, they had agreed expressly at the outset not to try the liability issue. As a consequence, there was neither any trial on the plaintiffs' allegations of oppression, nor any findings on the issue by the court. The matters that the court was called upon to resolve were purely tangential factual matters, and discrete legal issues that were not premised upon any finding of oppression on the part of the first and second defendants. Counsel for the plaintiffs was content to take this course of action, with the full knowledge that the court would be making no determination on the liability issue. On this footing, the plaintiffs should not have a second bite at the cherry simply because they were dissatisfied with the valuer's report, which the parties had expressly agreed would be final.

7.20 In *Ng Sing King v PSA International Pte Ltd (No 2)* [2005] 2 SLR 56 ("*Ng Sing King*"), the plaintiffs were minority shareholders in eLogicity International Pte Ltd ("eLogicity"). The first defendant was PSA International Pte Ltd ("PSAI"), a subsidiary of PSA Corporation ("PSA"). The second defendant, P&O Australia Pty Ltd ("POAP"), was owned by P&O Ports Ltd ("P&O"). In September 2000, PSAI and POAP (collectively, "the strategic shareholders") entered into a shareholders' agreement ("the

Shareholders' Agreement") with the plaintiffs, under which they acquired the majority of the shares in eLogicity, and were entitled to nominate directors to the company's board of directors. At the material time, the first plaintiff, Ng Sing King ("Ng"), was chairman of eLogicity's board of directors, and its chief executive officer ("CEO"). The second plaintiff, Lim Khoon Hock ("Lim"), was a director, and part of eLogicity's management.

7.21 The plaintiffs commenced proceedings against the strategic shareholders for alleged breaches of s 216 of the Act. First, it was alleged that the plaintiffs had been wrongfully excluded from negotiations between the strategic shareholders, their parent companies, and SAVI Technology Inc ("SAVI"), an American company that was a competitor of eLogicity. Upon the termination of Ng and Lim's employment, the strategic shareholders and their parent companies collaborated with SAVI. Second, the plaintiffs alleged that PSAI and POAP's nominee directors had participated in discussions for the formation of the Port Information Exchange ("PIE"), an organisation which would possibly be in direct competition with eLogicity. Moreover, POAP's Jonathan Ladd ("Ladd"), who was also a director of eLogicity, had negotiated on P&O's behalf with Hutchison Ports and Logistics Information Network Eneterprise ("HPH/LINE") and Stevedoring Services of America ("SSA") to invest in a "new eModal", which was akin to the PIE. This, it was alleged, constituted a breach of fiduciary duty to eLogicity on the part of Ladd. Third, the plaintiffs claimed that the strategic shareholders had systematically removed eLogicity's existing management, in order to put in place a new management that would comply with their instructions. It was also claimed that they had then decided to downsize eLogicity, in order to facilitate their pursuit of similar businesses with other parties. For relief, the plaintiffs prayed for the purchase of their shares by the strategic shareholders at fair value.

7.22 The strategic shareholders disputed these allegations, and instead sought the winding up of eLogicity pursuant to s 254 of the Act, on the grounds that it was just and equitable to do so. MPH Rubin J dismissed the plaintiffs' claim, and ordered the winding up of eLogicity.

7.23 In all actions alleging minority oppression, the courts must find a balance between two seemingly contrasting principles. The first is the general principle that corporations are run on the basis of majority rule. The majority of the shareholders, and the directors, are entitled to make decisions within the sphere of their responsibility. However, this is not an absolute rule, because there will be circumstances where majority rule becomes tyranny, and the law must provide a mechanism to curb the excesses of majority rule.

A failure to do so may undermine the utility of the company as a business vehicle, as potential investors may be less inclined to invest in companies in the complete absence of mechanisms to limit what, however unfair, the majority can do.

7.24 In *Ng Sing King* (*supra* para 7.20), this balance was recognised by Rubin J. His Honour said that the crucial question he had to consider was whether there was a visible departure from the standards of fair dealing, and a violation of the conditions of fair play which a shareholder was entitled to expect. There was a fine distinction, in this regard, between the legitimate rule of the majority, and tyranny of the majority. The mere fact that one or more of those managing the company possessed a majority of the voting power and, in reliance upon that power, made policy or executive decisions with which the complainant did not agree, was not enough in itself. Majority rule was the norm in many companies, and the exercise of majority power would inevitably cause dissatisfaction amongst minority shareholders. The court could not intervene merely because of disagreement amongst the shareholders, for the court was not a supervisory board over the decisions made by shareholders. Section 216 should therefore not be invoked by the court in order to interfere with the internal management of a company by directors who were acting honestly and who were not seeking to advance their interests, or the interests of others, at the expense of the company or contrary to the shareholders' interests. The plaintiffs might understandably have felt aggrieved, or even felt that they had been treated unfairly. Nonetheless, that sentiment alone was an insufficient basis for a successful application under s 216.

7.25 Rubin J also said that the court might consider whether the legitimate expectations of the minority shareholders had been disregarded. However, where parties had spelt out in detailed agreements all matters which were to govern their relationship, legitimate expectations would normally not arise apart from these agreements. However, it did not necessarily follow that any breach of an agreement was tantamount to oppressive conduct. Many other factors, and in particular, the harm caused by the breach, had to be considered in order to ascertain whether the breach resulted in unfairness, such as whether the breach was deliberate, whether it was a significant breach in disregard of a major expectation, and whether any detriment was caused to the aggrieved shareholder. Above all, the plaintiffs had the onus of showing that the breach prejudiced their interest in some way.

7.26 As regards the allegation that the plaintiffs had been wrongfully excluded from negotiations with SAVI, Rubin J held at [101] that the strategic shareholders' conduct could not be deemed "wrongful". The plaintiffs did not have any legitimate expectations, from the Shareholders' Agreement, of being included in all negotiations with SAVI. There was also no proof that the strategic shareholders, even if they had indeed excluded the plaintiffs, were motivated by an improper collateral motive. The strategic shareholders had sought to include eLogicity in an alliance with SAVI, and it was therefore reasonable to assume that they were seeking to further the interests of eLogicity. His Honour said that he would readily have found that there was an improper motive, if it could be shown that the alliance with SAVI was undeniably detrimental to eLogicity. He noted that there were both potential advantages, as well as disadvantages, to be reaped from the alliance. Consequently, there was an irreconcilable clash of views on the merits of an alliance with SAVI. The strategic shareholders were not pursuing a course of action that would invariably cause eLogicity's downfall. In such circumstances, the strategic shareholders' conduct could not be condemned as improper. They were merely seeking to further the interests of eLogicity by pursuing the alliance with SAVI.

7.27 On the allegation that the strategic shareholders had removed eLogicity's existing management, Rubin J held that the decision to terminate Ng's and Lim's employment was not unfair. The unambiguous terms of the Shareholders' Agreement precluded any understanding that Ng's position would be entrenched, or that the plaintiffs would be represented in the management. The strategic shareholders were entitled to remove Ng and Lim from management. In addition, the court found that, in entering into an alliance with SAVI, the strategic shareholders had been driven by a desire to alleviate the dismal state of affairs in eLogicity. There was nothing illegitimate in seeking to remove a CEO whom they perceived to be hindering their prospects of pursuing this plan, which they thought was in eLogicity's interest. Moreover, the alliance with SAVI was merely one of several factors that the strategic shareholders had taken into consideration when deciding to remove Ng. It was also not unreasonable for them to hold Ng responsible for the poor performance of eLogicity. Their decision was ultimately not made in bad faith

7.28 There was also no sinister motive underlying the strategic shareholders' decision to downsize eLogicity. There was insufficient evidence to conclude that their desire to collaborate with SAVI was the sole reason for this decision. On an objective analysis of eLogicity's performance, it was evident that the company was on the brink of atrophy, and that corrective

steps had to be taken. Downsizing the company seemed to be the most realistic course of action to take in order to minimise eLogicity's losses.

7.29 Although the PIE could have posed a competitive threat to eLogicity's business, there was meagre evidence to show that the PIE had actually come into being. With regard to the new eModal, even though Ladd's conduct in negotiating on behalf of P&O constituted a breach of his fiduciary duty to eLogicity, POAP was not vicariously liable for Ladd's breach of duty, since he had exceeded the scope of his responsibility as POAP's nominee director in eLogicity. Further, a breach of duty was not tantamount to oppressive behaviour unless it resulted in loss to the plaintiffs. HPH/LINE and SSA had cited other reasons for refusing to work with eLogicity, and might still have been keen to invest in the new eModal, with or without Ladd's involvement. Hence, Ladd's actions, while deplorable, had not caused the plaintiffs any loss.

7.30 On the strategic shareholders' petition to wind up the company, Rubin J accepted that there had been an irretrievable breakdown in the relationship amongst the shareholders, and that there was a loss of the substratum of the company. Either finding would have been sufficient to justify winding up the company on the just and equitable ground. It was clear that eLogicity's business had been crippled by endless disputes among the shareholders, and that they would no longer be able to work together. It was patently obvious, from the evidence considered above, that there were irreconcilable differences, and that the shareholders could no longer work together. The degree of acrimony among the shareholders was readily apparent from their conduct at the board meetings. Those meetings were disorderly and acrimonious, and the disputes amongst the shareholders hampered the calm discussion of urgent issues on the agenda. There was also evidence that the company was no longer viable, and that it was doubtful whether it could operate profitably. In the circumstances, it was just and equitable to wind up the company.

7.31 *Lim Swee Khiang v Borden Co (Pte) Ltd* [2005] 4 SLR 141 involved a case where a claim for relief under s 216 of the Act was dismissed after the defendants submitted that there was no case to answer. Judith Prakash J felt that the facts did not make out a case of oppressive conduct on the part of the majority.

7.32 Prakash J went on to say, however, that even if the plaintiffs had been able to satisfy her that they had been oppressed by the majority shareholders, they would have had difficulties in obtaining the relief that they were seeking.

The plaintiffs had asked the court to wind up the company concerned ("Borden"). They were not interested in buying out the defendants, or in being bought out by them. As a general proposition, where a company was doing well, the court would be reluctant to order it to be wound up. In the present case, the bigger obstacle that the plaintiffs faced in obtaining such relief was the allegation by the defendants that the action, or the continuation of the action, was an abuse of process.

7.33 Apparently, when the action was started on 9 September 2002, one of the prayers was that the second to tenth defendants be ordered to purchase the plaintiffs' shares at a price to be fixed by a valuer upon the completion of a re-audit by the plaintiffs' accountants. This was prayed as an alternative to the liquidation of the company. On 20 September 2002, the defendants' solicitors wrote to state that the defendants were willing to purchase the plaintiffs' shares, pursuant to a valuation by a professional valuer to be agreed upon between the parties. This offer was, in substance, the same as that prayed for except that the plaintiffs' prayer contemplated a re-audit of Borden's accounts by the plaintiffs' auditors. Further correspondence on this matter ensued between the parties, but ultimately the plaintiffs rejected all offers from the defendants to settle the matter along such lines.

7.34 Prakash J said that it was clear from the House of Lords case of *O'Neill v Phillips* [1999] 1 WLR 1092, that where there was a reasonable offer to purchase the allegedly oppressed party's shares, an action for oppression could not be sustained. In the present case, since the plaintiffs declined to engage in any discussions as to the mechanics of valuation, or as to any details of the valuation or offer, the issues of access to information and costs could not be addressed. Had the plaintiffs responded in a positive way to the defendants' offers, these issues could have formed part of the negotiations, and where the parties were unable to agree, the court could have made a decision on the point. The plaintiffs in this case had received an offer very shortly after the commencement of the action, but they did not do anything to try and resolve the situation notwithstanding that they themselves had asked the court to provide the terms upon which the shares could be bought out. It was only when the matter came to trial that the plaintiffs removed this prayer and stated that their sole aim was to achieve the winding up of the company. The learned judge said that she did not understand why the plaintiffs were so determined that Borden be wound up. The plaintiffs' attitude seemed to be that if they could not play an active part in the management of the company, it should cease to exist.

7.35 The company had an ongoing business. Its liquidation would result in a loss of the goodwill if its business could not be sold as a going concern. Even if a buyer could be found, forced sales did not generally result in full value being paid for the asset concerned. Whilst the plaintiffs' expert's position was that he required further documents and information in order to value the plaintiffs' shares, that did not mean that no valuation could be undertaken, since, if all parties co-operated in the exercise, more information should be forthcoming. In any case, an independent valuer would have done the best he could in the situation, and a procedure could have been worked out whereby certain issues affecting the valuation, being issues which could not be resolved by the valuer, could have been presented to the court for resolution.

7.36 Accordingly, Prakash J agreed that the plaintiffs were guilty of an abuse of process in continuing with the action, and in refusing to respond to the defendants' offer of a buyout. It was, however, too late to strike out the action, and the proper remedy was therefore a dismissal.

Company charges

7.37 A further issue that arose in *Pacrim* (*supra* at para 7.13) was whether a pledge of shares in the second defendant company, by the owner to the plaintiff, was a breach of the moratorium agreement against disposal of the shares that the owner had entered into with the second defendant company. The court held that a share certificate was not a documentary intangible, in that it was not the equivalent of the chose in action that the share it represented was. As such, the pledge of a share certificate did not confer on the pledgee the rights attaching to the shares, but only possessory title to the paper on which the share certificate was printed. Accordingly, where there was only a pledge of the share certificates, no interest in the shares they represented would thereby pass to the pledgee. Accordingly, there would be no breach of the moratorium.

7.38 Where, however, a blank transfer form duly executed by the registered shareholder was also deposited together with the share certificates upon the terms agreed between the owner and the plaintiff, what was created was not merely a pledge of the share certificates, but rather, the means whereby legal title to the shares might be transferred by completion and registration of such transfer. There is a long line of cases that have held that such an arrangement gives rise to an equitable mortgage over the shares because the intention is that the pledgee may, by completion of the blank transfer form, cause full title in the shares to be transferred to him, subject

only to an equity of redemption. Accordingly, Ang JC held that the arrangement entered into created an equitable mortgage, and not a mere pledge. As such, it was a breach of the moratorium.

Fraudulent trading

7.39 In *Tang Yoke Kheng v Lek Benedict* [2005] 3 SLR 263, the appellant brought an action against the respondents under s 340(1) of the Act. If this claim were made out, the persons who were knowingly a party to the fraudulent carrying-on of the company's business could be made personally liable for the debts of the company. Section 340(1) thus creates a statutory exception to limited liability. The company in question was Amrae Benchuan Trading Pte Ltd ("Amrae"), and the first and second respondents were its directors and shareholders. The third respondent was an employee of Amrae. The appellant traded in Bohemian crystalware under the name of "Niklex Supply Company" ("Niklex"), and was the principal supplier to Amrae.

7.40 In the course of time, Amrae came to owe substantial trade debts to the appellant. The appellant sued for the recovery of the debts, and a consent judgment was entered in 2002 against Amrae in the sum of $1,070,000. The appellant managed to recover $59,710.46 by way of a sheriff's sale, leaving the balance of the judgment debt unsatisfied. The appellant then obtained a winding-up order against Amrae on 19 September 2003. On 25 September 2003, the appellant commenced Suit No 864 of 2003 (the subject of the appeal). Various allegations of fraud were made. Ultimately, the appellant reduced her claim to the allegation that the three respondents had set up a company called Axum Marketing Pte Ltd ("Axum"), which they bought off the shelf in June 2001 and through which they began trading the following month; and that they had caused Amrae to transfer goods (purchased by Amrae from the appellant) to Axum. The total value of goods transferred by Amrae to Axum amounted to $1,268,983.02. The appellant's claim against the third respondent was for conspiracy, and the aiding and abetting of the s 340(1) offence by the first and second respondents.

7.41 In the course of the trial, the appellant adduced evidence to support her core allegation of the incidents and circumstances that she alleged constituted a breach of s 340(1) of the Act. The evidence was considered and evaluated by the trial judge, who formed the view that the evidence failed to prove fraud, and dismissed the appellant's action. The appellant appealed against that judgment. The appellant's principal contention was that the trial judge had failed to enquire into the most relevant issue, namely, whether Axum was created to be used as an instrument of fraud in that it was used to

profit the respondents by selling goods taken from Amrae without payment, thus leaving the appellant as the unpaid creditor of Amrae, and with no real recourse against Amrae. It should be said, though, that this submission did not take account of the fact that the liquidator of Amrae could cause that company to sue Axum for the debt owed to Amrae. If any moneys were recovered from Axum, the appellant would be entitled to a *pro rata* share of those moneys.

7.42 The business between the appellant and Amrae was conducted by the first and second respondents on behalf of Amrae, and by one Chan Chon Tuck ("Chan") on behalf of the appellant. The business relationship began in 1990, and spanned a period of ten years through 2000, during which time Amrae paid the appellant a total of about $5.2m in trade debts. In 1994, Chan asked the first and second respondents for a 50% stake in Amrae, on the grounds that Amrae owed him a huge debt on account of his generosity towards it in its business dealings with the appellant. The first and second respondents acceded to Chan's request, and eventually Chan was also given access to Amrae's books and financial records, which he inspected regularly. By 1998, the relationship between the first and second respondents and Chan was no longer the warm and trusting one they had shared before. It was about this time that the first and second respondents discovered that Chan had been charging exorbitant prices to Amrae for the goods supplied by the appellant. Chan was also unreliable in the delivery of goods ordered from the appellant. Consequently, as Amrae was not able to compete in the market, it ended with a $1.5m debt to the appellant. Notwithstanding this, Chan's interest in Amrae was increased to 70% in 1999, which the Court of Appeal thought strange.

7.43 From about February 2000, the first and second respondents also began to obtain supplies from other sources, and in June 2001, Axum was bought off the shelf to be used as a company through which the first and second respondents carried on their business. The evidence as to the reasons why the first and second respondents needed to have a new company (*viz*, Axum) appeared to be, first, a fear that the appellant might wind Amrae up because of the debts it owed to the appellant. There were also problems concerning the business relationship between Amrae and the appellant, mainly, it seemed, because the friendship between Chan and the first and second respondents was falling apart. That, in turn, led to disagreements as to how Amrae was to be run. Axum had, by the material time, paid up $713,831.38 of the debt it owed Amrae. The trial judge accepted that the money received by Amrae was used to pay directors' fees accrued over the years, rather than to pay the appellant. On these facts, the trial judge could

either infer that Amrae had indulged in fraudulent trading, or that it had merely exercised undue preference to one creditor over another. The trial judge inferred that the latter was the case.

7.44 The crux of the appellant's case as contained in the re-amended statement of claim averred that the first and second respondents, together with the third respondent, had incorporated Axum and caused Amrae to transfer to Axum goods bought from the appellant for the purported value of $1,268,983.02. No payments had since been made by Axum to Amrae.

7.45 In dismissing the appeal, the Court of Appeal said that to defraud someone was to commit an act or omission in which the fraudster deceived the innocent party so as to enrich the fraudster or cause the innocent party to suffer a loss or detriment. But the fraudster or cheat may achieve his objective in any number of ways. The only invariable element is the element of dishonesty on the part of the fraudster or cheat. Whether any given circumstances amounted to fraud was a question of fact to be determined by the court.

7.46 In determining whether there was dishonesty, the objective standard of what an honest person would have done in the circumstances was still a useful device to test the honest intention of the person concerned, against all the other evidence available, including, and especially, the explanation by the defendant of his deviation from what an honest person would have done in his circumstances. To rely on the objective standard as a sole test would be exceptional though, because it would require the court to treat any shortcomings from the objective standard as being sufficiently indicative of fraud as to warrant a finding of fraud.

7.47 On the standard of proof required, the court held that the civil standard of proving on a balance of probabilities applied where fraud was the subject of a civil claim, despite the infusion of a criminal element. However, because of the severity and potentially serious implications attaching to fraud, the court's expectation of proof would be higher even in a civil trial. The more serious the allegation, the more the party on whom the burden of proof fell had to do, in order to establish his case on a balance of probabilities.

7.48 The Court of Appeal found that there were at least two facts that might have warranted closer scrutiny and consideration. The first was that in a separate writ action, the appellant had sued Amrae in January 2001 for the unpaid price of goods. Given that the appellant's claim in the present action

concerned Amrae's conduct from July 2001 to June 2002, this meant that Amrae and the first and second respondents must have known for six months that there was a substantial claim against Amrae. *Prima facie*, an explanation would be required if assets were moved out of Amrae during this period. Amrae might have thought that the claim in the other action was frivolous and unsustainable, but if that were the case, it ought to explain why it consented to judgment. This point did not appear to have been raised at trial, and it did not feature in the court's judgment below. Furthermore, since the first and second respondents' case was that they started Axum because they had discovered that the appellant had overcharged Amrae, thereby making it no longer competitive, they ought to explain why it was that Axum bought goods from Amrae at a 10% higher price than what Amrae paid the appellant. However, the Court of Appeal was of the opinion that the rejection of fraud by the trial judge was not wrong because dishonesty and deception were key elements of fraud. From the record alone, the Court of Appeal did not think that Chan, the appellant's manager and key witness, could have been deceived when he had a 50% interest in Amrae (later increased to 70%), and had been diligently checking Amrae's profit and loss accounts and balance sheet, even though he claimed not to have seen the invoices and vouchers. If that finding of fact was wrong, it behoved the appellant to persuade the court on the evidence why the finding of those facts ought to be reversed. This had not been done. The trial judge had found no evidence of fraud against the third respondent. Nothing new was presented on appeal, and there was therefore no ground to disturb the trial judge's finding.