(2016) 28 SAcLJ 667
(Published on e-First 7 July 2016)

Case Note

RESERVE MANAGEMENT POWERS OF THE GENERAL MEETING

Chan Siew Lee v TYC Investment Pte Ltd
[2015] 5 SLR 409

Given the evolution of the division of powers between the board and general meeting over the years and devolution of significant management powers to the board, the Singapore Court of Appeal has, in *Chan Siew Lee v TYC Investment Pte Ltd* [2015] 5 SLR 409, declared its opinion on the doctrine of reserve management powers for the general meeting. It would appear from the decision that the issue of the general meeting's reserve management powers is effected through implication of the power on the basis of necessity. The Court of Appeal has provided guidance on how necessity is to be ascertained and new insights on the nature of the statutory contract.

LEE Suet Lin Joyce
LLB (Hons) (National University of Singapore),
LLM (University of Virginia);
Associate Professor, Nanyang Business School,
Nanyang Technological University.

1 The recent Singapore Court of Appeal case of *Chan Siew Lee v TYC Investment Pte Ltd*[1] ("*TYC*") had the occasion to consider the issue of whether the shareholders in a general meeting had reserve management powers and, if it did, the extent of the reserve management powers.

2 The Singapore Companies Act[2] has, over the years, variously assumed limited roles for the company's general meeting. Beyond the specific powers conferred on the general meeting under the Companies Act, the general meeting has the right to remove directors, and in cases where wrongs have been committed against the company, a member may, in limited circumstances, pursue these claims in a derivative action and seek a remedy for the company.

3 In addition, the general meeting may have specific powers conferred on it under the company's constitution. This sets out the

1 [2015] 5 SLR 409.
2 Cap 50, 2006 Rev Ed.

agreement that divides a company's power between the board and the general meeting. Both the board and the general meeting are generally regarded as "organs" of the company. The term "organ" ordinarily suggests the individual collective body's authority to act as the company, rather than as an agent which derives its authority from another corporate source. The doctrine of reserve management powers may hint at the board being an agent of the general meeting. Thus it is difficult to reconcile the doctrine of reserve management powers with the modern view[3] on the division of powers between the board and the general meeting, where each organ is regarded as sovereign and exercises powers conferred on it under the Companies Act and the constitution without interference from the other.

4 Given the evolution of the division of powers between the board and general meeting over the years and devolution of significant management powers to the board, it is timely that the Court of Appeal has declared its opinion on the doctrine of reserve management powers. It would appear from the decision that the issue of the general meeting's reserve management powers is effected through implication of the reserve management power on the basis of necessity. The Court of Appeal has also provided guidance on how necessity is to be ascertained.

I. The decision

5 The case involved a family holding company, TYC Investment Pte Ltd ("TYC"). The board consists of two directors, Henry Tay ("HT") and Jannie Chan ("JC"). HT and JC hold 46% and 44% of the voting rights in TYC. Their children hold the remaining 10% of the voting rights in TYC, with their son, Michael, holding 5% of the voting rights in TYC.

6 Articles 3 and 8 of TYC's articles of association confer on HT and JC extensive management powers as "permanent Governing Directors", including the power to appoint and remove fellow directors subject to the unanimous agreement of both HT and JC.

7 When HT and JC divorced in 2012, they entered into various agreements as part of their divorce settlement. TYC is a party to one of the agreements ("the TYC deed"). In addition, Art 16 of TYC's articles of association entrenches the terms of the TYC deed in the articles by

3 See, for instance, *Automatic Self-Cleansing Filter Syndicate Co Ltd v Cuninghame* [1906] 2 Ch 34.

stating that any amendment to the TYC deed requires the unanimous consent of all the shareholders of TYC.

8 HT and JC had agreed on a payment voucher system for TYC after JC was alleged to have made unauthorised payments out of TYC's bank accounts. A payment clause ("the Payment Clause") was included in an agreement to which TYC was bound and which provides as follows:

> Payment voucher system for all future payments for TYC. Neither [HT] nor [JC] will sign a cheque on TYC's bank accounts unless the other has signed a voucher approving.

9 JC subsequently relied on the payment clause to refuse to approve certain payments which HT wanted TYC to make. HT then called an extraordinary general meeting. Resolutions were passed by HT and Michael, who together hold 51% of the votes at the general meeting, to approve those payments which were withheld and to authorise HT to unilaterally sign cheques and vouchers to make payments on behalf of TYC. In addition, resolutions were passed to enable TYC to appoint solicitors and to commence proceedings against JC for various matters, one of which was for a declaration that the company's shareholders had reserve powers of management to approve specific payments where the board of directors was deadlocked.

10 The Court of Appeal held that whether there is a reserve management power vested in the general meeting depends on whether it is necessary to imply such a reserve management power. The concept of necessity is predicated on the condition that the board must be deadlocked or is unable or unwilling to act. If a management power is indeed to be reserved to the general meeting, its scope is limited only to the extent of what is necessary to enable the company to function.

11 Based on the fact that the board of TYC was deadlocked, the Court of Appeal ruled that it was necessary to imply a reserve management power for the general meeting to authorise payments to third parties but not to commence proceedings in the company's name.

II. Deadlock at the board

12 The Court of Appeal in *TYC* has stated categorically that reserve management powers will not be implied in favour of the general meeting unless the board is deadlocked. When reviewing the 11 cases cited by the High Court concerning deadlock, the Court of Appeal was of the opinion that only one case necessitated implying a reserve management power to the general meeting. With regard to the other ten cases, the Court of Appeal was of the view there were no "real or

intractable" deadlocks.[4] The bar as to what constitutes a deadlock is undoubtedly high, which means the cases where a reserve management power will be implied will be few and far between.

13 Among the cases which the Court of Appeal considered to involve no real or intractable deadlock was *Quin & Axtens Ltd v Salmon*[5] ("*Quin & Axtens*"), a case in which the Court of Appeal was of the view that the deadlock could have been resolved by reconstituting the board.

14 *Quin & Axtens* concerned a company that had two managing directors, Salmon and Axtens, who each held a substantial portion of the company's ordinary shares. Article 75 of the articles provided that the business of the company should be managed by the directors, who might exercise all the powers of the company "subject to such regulations (being not inconsistent with the provisions of the articles) as may be prescribed by the company in general meeting". Article 80 stated that no resolution of a meeting of the directors having for its object the acquisition or letting of certain premises should be valid if either Salmon or Axtens dissented. The directors resolved to acquire and to let various properties, but Salmon dissented. An extraordinary general meeting was then held at which the members, by a majority, passed a resolution to do the same. The House of Lords, upholding the decision of the Court of Appeal, held that the members' resolutions were inconsistent with the articles and granted an injunction restraining the company from acting on them. Lord Loreburn LC explained:

> The bargain made between the shareholders is contained in articles 75 and 80 of the articles of association, and it amounts for the purpose in hand to this, that the directors should manage the business; and the company, therefore, are not to manage the business unless there is provision to that effect. Further, the directors cannot manage it in a particular way – that is to say, they cannot do certain things if Mr Salmon or Mr Axtens objects. Now I cannot agree with Mr Upjohn in his contention that the failure of the directors upon the objection of Mr Salmon to grant these leases of itself remitted the matter to the discretion of the company in general meeting. They could still manage the business, but not altogether in the way they desired.

15 In *Quin & Axtens*, Art 80 permitted the board to act only if Salmon and Axtens did not object. As long as Salmon objected to the decisions to acquire and let the properties, even if the board were reconstituted with the addition of new directors, the board would still not be able to proceed. Two observations may be made about the case. First, the veto of Axtens and Salmon was effective only upon resolutions

4 *Chan Siew Lee v TYC Investment Pte Ltd* [2015] 5 SLR 409 at [49].
5 [1909] AC 442.

of the directors. Second, the veto was only in relation to acquisition and letting of certain premises pursuant to Art 80, and not in relation to the business of the company in general.

16 It is submitted, respectfully, that *Quin & Axtens* was not really a situation where new directors could be appointed to break the deadlock, since the decision had to be taken by the board, with or without additional directors, but together with Salmon and Axtens. It was a situation where the unique organ in question, the board and the two managing directors, had to come to a decision, and they did come to a decision regarding the leases, even if it was a decision against the wishes of everyone in the company except Salmon. As such, there was a real or intractable deadlock which could not be resolved by reconstituting the board, but not one which would allow the court to imply the general meeting had the power to do so, because the court would not imply a power which was contrary to the articles of association.

17 The Court of Appeal in *TYC* also dismissed *Barron v Potter*[6] ("*Barron*") and *Foster v Foster*[7] ("*Foster*") as cases where the deadlock could be broken by reconstitution of the board. *Barron* concerned a situation where the two directors of the company were not on speaking terms, so that effective board meetings could not be held. The plaintiff, Canon Barron, had requisitioned a members' meeting at which additional directors had purportedly been appointed. The defendant objected that the power to make such appointments was vested by the company's articles in the directors. It was held that, in view of the deadlock, the power in question reverted to the general meeting, and so the appointments were valid.

18 A similar decision was reached in *Foster* where there was a dispute over which of two directors should be appointed managing director. There were a total of three directors in the company. Although the power to appoint was conferred by the company's articles upon the directors, another article forbade a director from voting in respect of any contract in which he was interested. It was therefore not possible to carry any motion in view of the disqualification of one director and the opposition of another. Peterson J held that in those circumstances competence to deal with the matter reverted from the board to the general meeting.

19 It may be inferred from the Court of Appeal's treatment of these two cases that, even if a deadlock were to have arisen, the court may still

6 [1914] 1 Ch 895.
7 [1916] 1 Ch 532.

not imply the general meeting has reserve management power in relation to the issue that resulted in the deadlock, but will instead only imply the general meeting has reserve power to appoint additional directors to break the deadlock.

20 According to the Court of Appeal in *TYC*, the only case which might have necessitated the implication of a reserve management power to the general meeting is *Alexander Ward & Co Ltd v Samyang Navigation Co Ltd*.[8] In that case, the company had the usual article of association stating that business of the company was to be managed by directors. Summons and arrest of a vessel were issued, not by the directors, there being no directors in the company, but by persons without authority. The company subsequently went into liquidation. This was a case where there was no functioning board of directors, so the House of Lords accepted that the liquidator had the residual powers of the general meeting.

21 In addition, the Court of Appeal cautioned that there must also be enough shareholder votes to procure the passing of a resolution with the majority. This requirement that there be a functioning majority makes sense because once the management power is reserved to the general meeting, it must be able to exercise it by the passing of an ordinary resolution.

22 To sum up, it is clear from the Court of Appeal's decision that in order to qualify as a deadlock at the board and hence trigger the necessity to imply a reserve management to the general meeting, it must be a deadlock which cannot be broken by the appointment of additional directors. If necessary, the court may imply a reserve power to the general meeting to appoint additional directors, but not a reserve management power to the general meeting to decide on the issue that is at the heart of the deadlock. It must also be that, despite having a functioning general meeting that can pass an ordinary resolution, the majority is still not able to break the deadlock by appointing additional directors. Given these stringent conditions, cases which qualify as evidencing deadlocks will certainly be black swan events.

III. Claim may be resolved under s 216A

23 Where a claim can be resolved by a derivative action commenced under s 216A of the Companies Act, it may be argued that the power to commence litigation against the "wrongdoer" director either:

8 [1975] 1 WLR 673.

(a) should *not* be reserved to general meeting at all; or

(b) should be reserved to the general meeting, provided the requirements of necessity are satisfied.

24 The Court of Appeal in *TYC* took the middle ground, namely, that the court will scrutinise the facts of each case to consider whether s 216A provides an adequate remedy and, if so, whether it will still be necessary to imply a reserve power to commence litigation to the general meeting.

25 The argument that shareholders ought *only* to commence legal proceedings on behalf or in the name of the company under s 216A goes like this: where a management power was at issue, even assuming a deadlocked board prevented the exercise of that power, the shareholders in the general meeting could not exercise that management power. Section 216A would be the only appropriate avenue to force directors to act in the company's interests or to pursue the directors for a remedy, including for any loss suffered by the company due to their failure to act. Thus, the existence of s 216A will have the effect of breaking the deadlock on the board so that it is not necessary to imply a reserve management power to the general meeting to commence litigation. Directing shareholders to apply to court under s 216A is advantageous to the company because the shareholders would have to prove *prima facie* that they are acting in the interests of the company to commence litigation, which would not necessarily be the case if the decision were reserved to the general meeting, since shareholders are not constrained by fiduciary obligations to the company. This was JC's argument and the Court of Appeal rejected it because "it reaches too far".[9] The Court of Appeal explained the middle ground approach in these terms:[10]

> [T]he availability of s 216A will in certain circumstances *be relevant as a factor* in the overall analysis of whether it is necessary to imply a reserve power in favour of the shareholders as well as the terms and extent of such a power … the classic case where it will be appropriate to pursue a claim under s 216A is where it is directed against the very people who are otherwise empowered to decide on this such as where what is contemplated is an action for an alleged breach of the director's duties … There is good reason why such a matter will usually be best dealt with through this route rather than by implying a reserve power. The interposition of the court helps to reduce the possibility that the proceedings are being brought for tactical reasons stemming from corporate infighting rather than to address a genuine grievance that a director has acted in breach of his duties. [emphasis added]

9 *Chan Siew Lee v TYC Investment Pte Ltd* [2015] 5 SLR 409 at [57].

10 *Chan Siew Lee v TYC Investment Pte Ltd* [2015] 5 SLR 409 at [64].

26 The Court of Appeal appears to draw a distinction between a s 216A application to hold a director to account and one which does not. As regards disputes which do not hold a director to account, it was said that s 216A is not to be invoked where disgruntled shareholders aim to only challenge the business decisions of the directors. It was pointed out that were an action brought under s 216A to succeed, the remedy granted might only cure the current deadlock and not prevent further deadlocks. Shareholders cannot be expected to invoke s 216A and go through the process of getting leave and then taking the matter to trial each time there is a deadlock over the payment of a debt owed by the company to a third party. As regards disputes that hold a director to account, s 216A was said to be rightly invoked since the application is directed against the very people who are to decide on the litigation in the first place.

27 With respect, it is not entirely clear why a hearing to determine if a management power to commence litigation should be reserved for the general meeting is able to justify sending a plaintiff in that hearing away, based on what *may* happen in a s 216A application.

28 When the Court of Appeal in *TYC* pointed out the futility of using s 216A continuously to resolve a chronic deadlock at the board, it would appear the court was considering the probable outcome of such an application. That the reserve power to commence litigation will not be freely conferred on the general meeting can be seen from the stringent criterion of necessity. Since the Court of Appeal has already acknowledged that it will be a very rare case indeed where the concept of necessity applies, is it necessary to take that process one step further by putting s 216A in the "necessity" equation?

29 It is submitted, with respect, that instead of considering s 216A as part of the "necessity" equation, the reservation of power to commence litigation to the general meeting should coexist in parallel with the availability of s 216A.

30 First, the rule on reservation of power to commence litigation to the general meeting is a substantive issue and should not be conflated with the s 216A application, which essentially is a procedural issue. If the court were to rule that the shareholders have the reserve power to commence litigation against the director, a corporate action would be brought in the name of the company as plaintiff. The general meeting would be the competent organ to commence litigation if a reserve power was to be implied in its favour. Section 216A has its roots in the derivative action as exemplified by *Wallersteiner v Moir (No 2)*.[11]

11 [1975] 2 WLR 389.

31 If the substance of a claim were to be rejected, and in this context, that the general meeting does not have reserve power to commence litigation, then the reasons for rejecting the claim should be substantive in nature, rather than recourse being declared to be had to the availability or viability of another procedural device.

32 Second, that a reserve power of the general meeting to commence litigation coexists in parallel with other procedural devices which may be used by a shareholder to commence an action in the name of the company is supported by authority. The Court of Appeal in *TYC* cited *In re Argentum Reductions (UK) Ltd*[12] ("*Argentum Reductions*") for the principle that:[13]

> … a company should not needlessly be hamstrung by a deadlock on the board but should be allowed to get on with managing its affairs provided there is a functioning majority of shareholders.

33 The facts of *Argentum Reductions* are as follows. M held 48 of the 95 voting shares in a company and J the remainder. Their husbands constituted the board of directors which was in "an unhappy state of deadlock".[14] The company was being wound up but a motion was commenced under s 227 of the English Companies Act 1948[15] asking the court to validate what would otherwise have been a void disposition of company property, the action being commenced in the name of M, her husband and the company, and resisted by J and her husband. The decision of Megarry J was that M, as majority shareholder, had *locus standi* to make an application to the court under s 227.

34 Megarry J did not think it was necessary to consider the question of whether M had authority to commence a derivative action in the name of the company. This is because, where the board was in a deadlock, the general meeting's reserve power to sue in the company's name revived. The court could give the general meeting, if necessary, an opportunity to decide, and any problem as to quorum or other procedural requirements caused by J's refusal to attend the shareholders' meeting could be cured by an application to the court under the equivalent of s 182 of Singapore Companies Act.

35 With respect, it is submitted that once the conditions for necessity which are laid down by the Court of Appeal in *TYC* are fulfilled, the reserve power of the general meeting arises, regardless of the availability of s 216A. Both avenues, be it a functioning general

12 [1975] 1 WLR 186.
13 *Chan Siew Lee v TYC Investment Pte Ltd* [2015] 5 SLR 409 at [44].
14 *In re Argentum Reductions (UK) Ltd* [1975] 1 WLR 186 at 190.
15 c 48.

meeting seeking a court order that it has reserve management power or a shareholder making a s 216A application to redress a wrong to the company occasioned by the deadlocked board, serve their respective functions and the prospect of both avenues coexisting in parallel with each other at all times, it is submitted, is both correct in principle and supported by authority.

IV. Nature of statutory contract

36 The Court of Appeal's implication by necessity approach appears to signify a fundamental shift in the traditional understanding of the constitution as a compact between the board and the general meeting. The Court of Appeal's decision brings to the fore the nature of the statutory contract enshrined in s 39 of Companies Act.

37 In coming to the decision that the general meeting has a reserve management power to authorise payments, the Court of Appeal opined:[16]

> Undoubtedly, in the ordinary case, that decision is a matter for the board, but where the directors are deadlocked and it becomes apparent that the obligation owed by the company is *bona fide* and in the interests of the company to be honoured, then it seems to us that a reserve power may be implied to the shareholders to make that decision if this is necessary to do; and if this may be implied, then we cannot see how it can be said that the Payment Clause can nonetheless pose an insuperable obstacle to carrying out that decision. To put it another way: *the Payment Clause could not meaningfully stand in the way of a legitimately authorised liability of the company being met once the shareholders pursuant to and within the limits of a reserve power had determined that it should be met*. [emphasis in original]

38 The Court of Appeal in *TYC* has provided new insights into the nature of the statutory contract in two ways. First, the interests of persons outside the company are taken into consideration to determine if a management power should be reserved to the general meeting to enable the company to function. Second, a reserve management power to the general meeting may be implied even if it is contrary to an express provision in the statutory contract.

39 The Court of Appeal explained their decision to consider the interests of persons outside of the company in the following manner:[17]

> It is true that the court, when confronted with the issue of the shareholders' reserve powers, is dealing with an issue of the

16 *Chan Siew Lee v TYC Investment Pte Ltd* [2015] 5 SLR 409 at [77].
17 *Chan Siew Lee v TYC Investment Pte Ltd* [2015] 5 SLR 409 at [47].

> management of the company's affairs and the balance of powers between the (usually competing) shareholders on the one hand and the (usually divided) board on the other; yet in determining that issue, it is plainly right that the interests of innocent creditors will have to be considered and will often have a bearing on how the court should strike a balance among the competing factions whose disputes *within* the company threaten to paralyse the company and prejudice innocent third parties *outside* it. [emphasis in original]

Thus, when considering the balance of powers between general meeting and the board, the court considers whether the company functions, not only internally, but externally *vis-à-vis* third parties.

40 The Court of Appeal's approach in *TYC* is noteworthy because it has moved away from the traditional notion that the only "constituents" of a company are its members. The traditional view ignores the claims of employees, management, creditors and other stakeholders whose interests in the company and its constituents are also significant. Thus, the constitution has traditionally always been shackled by defining it in terms of several relationships, namely, the company and members as parties to the statutory contract,[18] and the members as parties to the statutory contract *vis-à-vis* each other.[19] The classical approach to the constitution was so restrictive it even generated a controversy of whether a member may enforce *all* the provisions in the statutory contract or only "*qua* member" rights.[20] By taking a pragmatic approach to ascertaining if the provision in question affects the power of the company to *function*, one may surmise that the Court of Appeal is concerned not so much about whether a provision in the statutory contract contains a *qua* member or outsider right but rather about how to balance the interests of the stakeholder constituents of the company.

41 In addition, it is also interesting that in spite of the fact that TYC had been set up with a structure in which a deadlock is a distinct possibility, the court did not view the express provision as an impediment to reserving management powers in favour of the general meeting.

42 In *Imperial Hydropathic Hotel Co, Blackpool v Hampson*[21] the articles provided that the directors were to hold office for a period of three years and to retire by rotation. The general meeting passed resolutions to remove two directors who were not due for retirement

18 *Hickman v Kent or Romney Marsh Sheep-Breeders' Association* [1915] 1 Ch 881.
19 *Rayfield v Hands* [1960] Ch 1.
20 *Eley v Positive Government Security Life Assurance Co Ltd* (1876) 1 Ex D 88.
21 (1882) 23 Ch D 1.

under the articles and the election of others in their place. According to Cotton LJ:[22]

> Now in my opinion it is an entire fallacy to say that because there is power to alter the regulations, you can by a resolution which might alter the regulations, do that which is contrary to the regulations as they stand in a particular and individual case. It is in no way altering the regulations. The alteration of the regulations would be by introducing a provision, not that some particular director be discharged from being a director, but that directors be capable of being removed by the vote of a general meeting. It is a very different thing to pass a general rule applicable to every one who comes within it, and to pass a resolution against a particular individual, which would be a *privilegium* and not a law.

The case stands for the proposition that where the articles limit the powers of the company in a general meeting, such articles cannot be disregarded even by a majority sufficiently large to alter the articles. A formal alteration must be made and then acted upon.

43 According to this classical approach, it is by the consensus of *all* the members of the company that HT and JC became entrenched as directors of TYC and indirectly entrenched the payment clause in the constitution of TYC. The classical approach would not permit a majority at a meeting that is called for the purpose of deciding the payment issue to alter the mandate given under the constitution to the directors jointly.

44 It would appear that the Court of Appeal, in deriving a reserve management power through necessity, which is referable to the interests of the company to honour *bona fide* obligations to the company's creditors and which can override an express provision in the constitution, has moved away from the traditional view of the statutory contract as a discrete set of static obligations between the company and its members. It is submitted, with respect, that it is timely that the Court of Appeal has chosen to move away from the traditional view of the statutory contract and come to view it as a framework of ongoing set of dynamic relationships between the company and various stakeholders.

V. Conclusion

45 The law keeps pace with commercial practice in recognising that general management of the company is ordinarily vested in the directors. It is clear from *TYC* that the doctrine of reserve management powers of the general meeting can be invoked only where the board is deadlocked. Yet, the conditions to be satisfied to qualify the board as

22 *Imperial Hydropathic Hotel Co, Blackpool v Hampson* (1882) 23 Ch D 1 at 3.

deadlocked are stringent and so the doctrine will be seldom invoked. The Court of Appeal's "stakeholder" approach to the constitutional division of powers between the board and the general meeting signals a bold and opportune departure from the way the statutory contract is looked at traditionally.
