CONTROLLING SHAREHOLDERS AND FIDUCIARY DUTIES IN COMMON LAW ASIA

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ABSTRACT

This thesis is the first monograph to provide a critical and comparative examination of the question of why, when, by whom, and how fiduciary duties should be imposed on controlling shareholders in the listed companies in the four common law jurisdictions in Asia (Singapore, Hong Kong, Malaysia and India) as well as how those duties can be enforced. Because different ownership structures (i.e. dispersed versus concentrated) give rise to different corporate governance problems (i.e. separation of ownership and control versus extractions of private benefits of control), the question is whether the four Asian jurisdictions should depart from the current UK legal position (on which their laws are based)—shareholders do not owe fiduciary duties to the company—and impose such duties on the controlling shareholders. This thesis provides an affirmative answer and seeks to make three contributions. First, this thesis calls into question a long-standing, fundamental legal principle that shareholders unlike directors, should not owe fiduciary duties to the company as they can vote as they please and they are not agents. Second, this thesis deepens the existing analysis of the strategies that have been used to address extractions of private benefits of control by controlling shareholders by demonstrating that they are not only deficient, but they also fail to regulate other types of conflicts of interest which can give rise to tunneling. Finally, this thesis advances the debate on a central and fundamental concept in corporate law and governance—the interests of the company—from a normative, legal and empirical perspective by showing that corporate interest need not be equated with shareholders' or stakeholders' interests, but could refer to the long-term value and viability of the company.

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TABLE OF ABBREVIATIONS

HK CO	Hong Kong Companies Ordinance (Chapter 622)
HKEX GEM LR	Hong Kong Stock Exchange Growth Enterprise Market Listing Rules
HKEX LR	Hong Kong Stock Exchange Listing Rules (Main Board)
IN CA	India Companies Act 2013
MY CA	Malaysia Companies Act 2016
Bursa Malaysia LR	Bursa Malaysia Listing Requirements (Main Market)
SEBI LODR	Securities and Exchange Board of India Listing Obligations and Disclosure Requirements
SG CA	Singapore Companies Act (Chapter 50) Revised ed 2006
SGX LR	Singapore Exchange Listing Rules (Main Board)

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Shareholder Power	**Hong Kong**		**Singapore**		**India**		**Malaysia**		**UK**	
	Provision(s)	Ordinary Resolution (OR)/Special Resolution (SR)	Provision(s)	Ordinary Resolution (OR)/Special Resolution (SR)	Provision(s)	Ordinary Resolution (OR)/Special Resolution (SR)	Provision(s)	Ordinary Resolution (OR)/Special Resolution (SR)	Provision(s)	Ordinary Resolution (OR)/Special Resolution (SR)
Appointment of directors	Art. 23(1)(a) (Sch 1 Companies (Model Articles) Cap 622H)	OR	S. 149B (Singapore Companies Act) (Cap 50)	OR	s. 152 (India Companies Act 2013)	OR	s. 202(2) (Malaysia Companies Act 2016) (Act 777)	OR	Art 20(a) (Companies (Model Articles) Regulations Regulation 4, Sch 3)[1]	OR
Removal of directors	s. 462 (Hong Kong Companies Ordinance) (Cap 622)	OR with special notice	s. 152 (Cap 50)	OR with special notice	s. 169 (India Companies Act 2013)	OR with special notice	s. 206(2) (Act 777)	OR with special notice	s. 168(1) (Companies Act 2006)	OR with special notice
Alteration of articles	s. 88(1) (Cap 622)	SR s.88(2) (Cap. 622)	s. 26(1) (Cap 50)	SR	s. 13(1) s. 14(1) (India Companies Act 2013)	SR	s. 36(2) (Act 777)	SR	s. 21(1) (Companies Act 2006)	SR
Requesting directors to hold general meeting	s. 566 (Cap 622)	Requisition by members holding not less than 5% of the total voting rights	s. 176(1) (Cap 50)	Requisition by members holding not less than 10% of total number of paid up shares or if the company has no share capital, at least 10% of the total voting rights	s. 100(2) (India Companies Act 2013)	Requisition by members holding not less 10% of total paid up share capital or if the company has no share capital, at least 10% of the total voting rights	s. 311(3) (Act 777)	Requisition by members holding not less than 10% of total paid up capital or if the company has no paid up capital, at least 5% of the total voting rights	s. 303(2) and (3) (Companies Act 2006)	Requisition by members representing at least 5%[2] of total paid up capital of the company as carries the right of voting at general meetings of the company
Calling general meeting (without asking directors)	s. 569 (Cap 622)	When a company does not have any director or does not have sufficient directors capable of acting to form a quorum, any 2 or more members of the company representing at least	s. 177 (Cap 50)	Two or more members holding not less than 10% of the total number of issued shares of the company or, if the company has no share capital, not less	/	/	s. 310(b) (Act 777)	Any member holding at least 10% of the issued share capital of a company or a lower percentage as specified in the company's constitution or if the company has no share capital, by at	/	/

[1] The Companies (Model Articles) Regulations 2008, see Reg 4, which states that for s303(2) (a) and (b) of the Companies At 2006, the required percentage becomes "5%" and s. 303(3) is omitted.

[2] The required percentage has been reduced from 10% to 5% by The Companies (Shareholders' Rights) Regulations 2009.

		10% of the total voting rights of all the members having a right to vote at general meetings, may call a general meeting		than 5% in number of the members of the company or such lesser number as is provided by the constitution may call a meeting of the company				least 5% in the number of members may call a meeting of members		
Directing directors to take/refrain from taking action	Art 3(1) (Sch 1 Cap 622H)	SR	/	/	/	/	s. 195(3)(b) (Act 777)	SR[3]	Art 4(1) (Regulation 4, Sch 3)	SR
Exercise management power	Art 3(1) (Sch 1 Cap 622H) Article 2(1) (Sch 1 Cap 622H)	By directing directors to take certain actions Directors' power are subject to the Articles of the company. Note that shareholders can alter the Articles of the Company under s.88(1) of the Companies Ordinance (Cap 622) and reserve management powers	s. 157A(2) (Cap 50)	The directors may exercise all the powers of a company except any power that this Act or the constitution of the company requires the company to exercise in general meeting. Note that shareholders can alter the Articles of the Company s.26(1) of Cap 50 and indirectly reserve management powers.	s. 179(1) (India Companies Act 2013)	The Board shall be subject to the provisions contained in the Act, or in the memorandum or articles, or in any regulations not inconsistent therewith and duly made thereunder, including regulations made by the company in general meeting. Note that shareholders can alter the Articles of the company under s.13(1) and s.14(1) of the Companies Act and indirectly reserve management powers.	s. 211(2) (Act 777)	The Board has all the powers necessary for managing the affairs of the company subject to any modification, exception or limitation contained in the Companies Act or in the constitution of the company. Note that shareholders can alter the Articles by s.21 of Act 777 to indirectly reserve management power	Art 3 (Regulation 4, Sch 3)	Directors' management powers are subject to the Articles of the company. Note that shareholders can alter the Articles under s.21(1) of the Companies Act 2006 to indirectly reserve management power.
Ratifying breach of duties by the directors	s. 473(1) (Cap 622)	OR[4] s.472(2) (Cap 622)	Common Law[5]	/	Common Law[6]	/	Common law[7]	/	s. 239(2) (Companies Act 2006)	OR[8]

3 If the company constitution does not provide for the right, a SR is required.

4 The votes of the director(s) in breach of his duties and any members connected to him should be disregarded

5 *Raffles Town Club Pte Ltd v Lim Eng Hock Peter* [2013] 1 SLR 374 at [45]

6 *Balasaraswathi Limited Tirunelveli v A. Parameswara Aiyar* AIR 1957 MAD 122 at [18]

7 *Teoh Peng Phe v Wan* [2001] 1 AMR 358

8 The votes of the director(s) in breach of his duties and any members connected to him should be disregarded (s.239(4) of Companies Act 2006)

Approving mergers (scheme of arrangement)	s. 674(2) (Cap 622)	SR[9]	Part VII (Cap 50)	(i) scheme of arrangement: SR s.210(3AB)[10]/ (ii) amalgamation proposal: SR[11] s.215C(1)(a) Additional requirements may be imposed by SGX[12]	s. 230 (India Companies Act 2013)	SR[13] s.230(6) Companies Act 2013	s. 366(2) (Act 777) Schedule 3 of the Rules on Take-overs, Mergers and Compulsory Acquisitions	SR[14] SR[16] Rule (2)(f) of Schedule 3	s. 907(1) (Companies Act 2006)	SR[15]
Approving M & A (non scheme of arrangement)	Rule 30.2 Codes on Takeovers and Mergers and Share Buy-back Rule 30.2	Voluntary Offer No resolution is required. Voluntary offers would be subject to any acceptance condition (min. 50% acceptances). As long as the acceptance condition is satisfied within specified time e.g. conditional on 90% acceptances, transaction will take place.	Rule 15.1 The Singapore Code on Takeovers and Mergers Rule 14.2(a) The Singapore Code	Voluntary Offer No resolution is required. A voluntary offer must be conditional upon the offeror receiving acceptances in respect of voting rights which, together with voting rights acquired or agreed to be acquired before or during the offer, will result in the offeror and person acting in concert with it holding more than 50% of the voting rights.	Rules 3-6, 19 SEBI (Substantial acquisition of shares and takeovers) Regulations, 2011	Voluntary Offer No resolution is required. The offer may be conditional upon a minimal level of acceptance as fixed by the acquirer.	Rule 6.01(2) Rules on Takeovers, Mergers and Compulsory Acquisitions Rule 6.01(1)	Voluntary Offer No resolution is required. A voluntary offer must be conditional upon the offeror having received acceptances which would result in the offeror holding in aggregate more than 50% of the voting shares or voting rights of the offeree.	Voluntary Offer Section G Rule 10 The City Code on Takeovers and Mergers	Voluntary Offer No resolution is required. Voluntary offers: subject to any acceptance condition above 50% acceptances.

9 s. 674(2) and Rule 2.10(a) of the Codes on Takeovers and Mergers and Share Buy-Backs require a resolution passed by (i) members representing at least 75% of the voting rights of the members present and voting, in person or by proxy AND (ii) the votes cast against the arrangement at the meeting do not exceed 10% of the total voting rights attached to all disinterested shares in the company

10 It requires a resolution passed by (i) a majority in number of members present and voting either in person or by proxy at the meeting AND (ii) members agreeing to the scheme represent three-fourths in value of members present and voting either in person or by proxy at the meeting

11 It requires a resolution passed by the members of each amalgamating company by special resolution at a general meeting

12 Under rule 106 of the Mainboard Rules SGX-ST Listing Manual, SGX may impose an additional requirement on listed companies that not more than 10% in value of the shares should have voted against the proposed scheme. The acquirer and its related parties are not allowed to vote.

13 It requires a resolution passed by majority of persons representing three-fourths in value of members voting in person or by proxy or by postal ballot

14 It requires a resolution passed by a majority of 75% of the total value of members present and voting either in person or by proxy at the meeting

15 The scheme must be approved by a majority in number, representing 75% in value, of each class of members of each of the merging companies, present and voting either in person or by proxy at a meeting

16 It requires a resolution passed by (i) members representing at least majority in numbers and 75% in value to the votes attached to the disinterested shares that are cast either in person or by proxy at a duly convened shareholders' meeting AND (ii) the value of votes cast against the resolution for the scheme at such duly convened shareholders' meeting is not more than 10% of the votes attaching to all disinterested shares of the total voting shares of the offeree.

	Codes on Takeovers and Mergers and Share Buy-back	<u>Mandatory Offer</u> No resolution is required. All mandatory offers are subject to a 50% acceptance condition[17]. As long as the acceptance condition is satisfied, the offer will go ahead.	on Takeovers and Mergers	<u>Mandatory Offer</u> No resolution is required. All mandatory offers are subject to a 50% acceptance condition.		<u>Mandatory Offer</u> No resolution is required.	Rules on Takeovers, Mergers and Compulsory Acquisitions	<u>Mandatory Offer</u> No resolution is required. All mandatory offers are subject to a 50% acceptance condition.	Mandatory offer Rule 9.1 Rule 9.3 Acceptance Conditions The City Code on Takeovers and Mergers	<u>Mandatory Offer</u> No resolution is required. All mandatory offers are subject to a 50% acceptance condition
Approving directors' loan	s. 500 (Cap 622)	OR (by disinterested members[18])	s. 162(4) (Cap 50)	OR (by disinterested members[19])	s. 185(a)(ii) (India Companies Act 2013)	SR	s. 224(3) (Act 777)	OR (by disinterested members[20])	s. 197(1) (Companies Act 2006)	OR (by disinterested members[21])
Approving related party transactions	LR 14A.36 (Listing Rules of the Stock Exchange of Hong Kong)	Disinterested shareholder approval[22]	LR 906, LR 918 LR 919 (SGX-ST Listing Manual)	Disinterested shareholder approval[23]	Reg 23(4) of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015[24] s. 188(1) (India Companies Act 2013)[25]	Disinterested shareholder approval	s. 228(2)(a) (Act 777) LR 10.08(2)(b), 10.08(7)(a) (Main Market Listing Requirements of Bursa Malaysia)	OR Disinterested shareholder approval[26]	LR 11.1.7(4) (UKLA Listing Rules)	Disinterested shareholder approval[27]
Approving significant transactions	LR 14.06(3), LR 14.40, LR 14.44,	Disinterested shareholder approval If any percentage	Major Transactions LR 1014(2)	OR if any percentage ratio	s. 180(1) (India Companies Act	SR If the transaction involves a disposal of	LR 10.07(1)(b) (Main Market	OR If any percentage	LR 10.2.2(3) Class 1 Transactions	If any percentage ratio of the transaction > 25%

17 together with shares acquired or agreed to be acquired before or during the offer, will result in the offeror and persons acting in concert with it holding more than 50% of the voting rights of the offeree company.

18 If any of the size test ratios in relation to the loan is more than 5% or if the loan was not made on normal commercial terms or better to the listed issuer, rule 14A.36 of the Listing Rules of the Stock Exchange of Hong Kong requires that any shareholders with material interest in the transaction must abstain from voting.

19 If the amount of loan is equivalent to or more than 5% of the group's latest audited net tangible assets or 5% of the group's latest audited net tangible assets, when aggregated with other transactions entered into with the same interested person during the same financial year, rule 919 of the Mainboard Rules SGX-ST Listing Manual requires that the interested person and his associates must not vote on the resolution.

20 If any one of the percentage ratios of the loan is 5% or more, rule 10.8 of the Main Market Listing Requirements of Bursa Malaysia requires that the interested person or his related parties must not vote on the resolution.

21 For non-exempt directors' loans, rule 11.1.7(4) of the UKLA Listing Rules requires that the related parties and their associates must not vote on the resolution.

22 Shareholder approval is exempted for de minimis transactions. See rule 14A.76(2) of Listing Rules of the Stock Exchange of Hong Kong.

23 A listed company must obtain shareholder approval for any interested person transaction of a value equal to, or more than (a) 5% of the group's latest audited net tangible assets; or (b) 5% of the group's latest audited net tangible assets, when aggregated with other transactions entered into with the same interested person during the same financial year. (rule 919 of the Mainboard Rules SGX-ST Listing Manual) The interested person and his associates must not vote in the resolution.

24 Shareholder approval is required when the related party transaction is a material transaction, i.e. exceeds 10% of the annual consolidated turnover of the listed entity.

25 For other related party transactions, shareholder approval is required when they are either not in the ordinary course of business or not at arm's length

26 If the percentage ratios of a related party transaction is 5% or more, rule 10.8 of the Main Market Listing Requirements of Bursa Malaysia requires that shareholder approval must be obtained. The interested person and his associates must not vote in the resolution.

27 Shareholder approval is exempted for small transactions where each of the applicable percentage ratios is equal to or less than 5% (Listing Rule 11.1.10).

	LR 14.46 (Listing Rules of the Stock Exchange of Hong Kong)	ratio of the transaction > 25%	Very Substantial Acquisitions or Reverse Takeovers LR 1015(1)(b) (SGX-ST Listing Manual)	of the transaction > 20%	2013)	an undertaking > 20% of its net worth as per the audited balance sheet of the preceding financial year, or an undertaking which generates 20% of the total income of the company during the previous financial year[28]	Listing Requirements of Bursa Malaysia)	ratio of the transaction > 25%	Class 2 Transactions LR 10.5.1 (UKLA Listing Rules) LR 10.4	Between 5 to 25% OR (For Class 1 Transactions) No requirements on shareholder's approval for Class 2 Transactions
Executive compensation	Art 28(1) (Sch 1 Cap 622H)	Director's remuneration must be determined by the company at a general meeting[29]	s. 169 (Cap 50)	Director's Emoluments - OR - binding[30]	s. 197(4) s. 197(1) Schedule V Section II (India Companies Act 2013)	The remuneration payable to the directors of a company, including any managing or whole-time director or manager - OR If the total managerial remuneration payable by a public company, to its directors, including managing director and whole-time director, and its manager in respect of any financial year exceeds 11% of the net profits of that company for that financial year - shareholder approval (OR) + approval by central government Where in any financial year during the currency of tenure of a managerial person, a company has no profits or its profits are inadequate, it may, without Central Government approval, pay remuneration to the managerial person not exceeding the	s. 230(1) (Act 777)	The fees and benefits of directors of public companies, listed companies and subsidiaries of listed companies must be approved by shareholders at general meeting.	s. 439(1) (Companies Act 2006)	Director Remuneration Policy - OR- binding Annual Remuneration Report - OR - advisory

28 Further this requirement applies if 20% or more of the undertaking referred to above is sought to be sold, leased or disposed off.

29 Therefore director's remuneration is subject to shareholder approval at general meeting. However, in the absence of similar articles in the company's articles of association, there is no mandatory legal requirement for director's remuneration to be approved by shareholders.

30 If the director receives remuneration as an employee of the company (that is, his salary is set out in his service contact, rather than being received as a fee "in respect of his office"), that remuneration need not be approved by the shareholders or disclosed in the company's accounts and is treated as a board matter.

						higher of the limits prescribed. The limit shall be doubled if a special resolution is passed.				
Inspection of documents	s. 740(6) (Cap 622)	On the application of members that represent at least 2.5% of the voting rights of all the members having a right to vote at the company's general meetings at the date of application; or at least 5 members of the company, court may authorise members to inspect record/documents of the company	Inspection of Books Of Corporation s.8A Inspection of Minute Books s.189(1) Inspection of Records s.396A Court may compel compliance s. 399(1) (Cap 50)	If any person in contravention of this Act refuses or fails to permit the inspection of any register, minute book or document or to supply a copy of any register, minute book or document the Court may by order compel an immediate inspection of the register, minute book or document or order the copy to be supplied.	s. 119(b) Inspection of Minute Books of General Meeting s. 171(1)(a) Members Right to Inspect s. 85(2)(a) Companies' Registrar of Charges s. 94(2) Register and Returns s. 189(3) Register of Contracts and Arrangements s. 190(2) Contract of employment with directors s. 187(3) Register of shares and securities s. 186(10) Register of Loan, Guarantee and Security	Company documents, such as minute-books, register of directors and their shareholding, register of charges, Register of members, debenture holders, annual returns, register of contracts in which directors are interested, contracts of employment with directors, investment of company to be held in its own name, loans and investment made by the company without charge or for any prescribed fee. If inspection is refused -	s. 585 (Act 777)	On the application of any member, the Court may by order require any officer/person to permit inspection of any register, minute book or document, or to supply a copies of these documents.	s. 118(3) Inspection of Register of Members s. 162(8) Register of Directors s. 229(5) Copy of Memorandum s. 275(8) Register of Secretaries s. 746(3) Register of Debenture Holders s. 813(3) Register of Interests s. 877(7) Register of Charges	In the case of any refusal or default, the Court may by order compel an immediate inspection of register of members, register of directors, directors' service contracts, register of secretaries, register of debenture holders, register of interests, register of charges/instrument creating charges or, as the case may be, direct that the copy required to be sent to the person requesting it.

					s. 119(4) s. 171(2) s. 94(5) (India Companies Act 2013)	The National Company Law Tribunal may by order direct an immediate inspection of the minute-books or direct that the copy required shall forthwith be sent to the person requiring it. The Registrar shall on application made to him order immediate inspection of the register of directors, key managerial personnel and their shareholding or supply copies required thereunder. The Central Government may also, by order, direct an immediate inspection of the register of members, debenture holders and annual returns, or direct that the extract required shall forthwith be allowed to be taken by the person requiring it				
Alteration of company: from public to private	s. 88(2) s. 95 (Cap 622)[31]	SR	s. 31(1) (Cap 50)	SR	s. 13 s. 14 (India Companies Act 2013)	SR	s. 41(1) (Act 777)	SR	s. 97(1)(a) (Companies Act 2006)	SR[32]

31 Alteration of status of the company is effected by an alteration of the Articles of the company under Part 3 Division 2 Subdivision 4 of the CO

32 S. 98(1)(a) provides that where a special resolution by a public company to be re-registered as a private limited company has been passed, an application to the court for the cancellation of the resolution may be made— (a) by the holders of not less in the aggregate than 5% in nominal value of the company's issued share capital or any class of the company's issued share capital (disregarding any shares held by the company as treasury shares); (b) if the company is not limited by shares, by not less than 5% of its members; or (c) by not less than 50 of the company's members; but not by a person who has consented to or voted in favour of the resolution.

Issues of shares	s. 141(1)(a)(i) (Cap 622)	OR	s. 161(1) (Cap 50)	OR	s. 62 (India Companies Act 2013)	SR/No approval required[33]	s. 75(1) (Act 777)	OR	s. 551(1) (Companies Act 2006)	OR
Or Disapplication of pre-emption right on issuance	LR 13.36(1)(a)(i) (general mandate) LR 19A.38 (PRC issuers) (general mandate) (Listing Rules of the Stock Exchange of Hong Kong)	OR SR	LR 804-805 (prior shareholder approval) LR 806(1) (general mandate) (SGX-ST Listing Manual)	OR (by disinterested members)[34] OR[35]/SR[36]	s. 62(1)(c) (India Companies Act 2013)	SR	LR 6.03-6.04 (general mandate) LR 6.05(a) (Main Market Listing Requirements of Bursa Malaysia)	OR LR 6.03(1) OR (prior shareholder approval needed if the issue of shares or other convertible securities departs from any of the requirements stipulated in Para 6.04	ss. 570(1)-571(1) (Companies Act 2006)	SR
Reduction of share capital	ss. 211, 217 (supported by solvency statement) s. 226(1) (confirmed by Court) (Cap 622)	SR (by disinterested members) s.217 (Cap 622) SR	s. 78C(1) (supported by solvency statement) s. 78G(1) (subject to approval by court) (Cap 50)	SR SR	s. 66 (India Companies Act 2013)	SR	s. 116(1) (confirmed by the Court) s. 117(1) (supported by solvency statement) (Act 777)	SR SR	s. 641(1)(a) and (b), 645(1) (confirmed by the court) (Companies Act 2006)	SR
Or Repurchase of shares	s. 238(1) (buy-back by general offer) s. 239(1) (market purchase) s. 240(1) (listed company buy-back shares under contracts) ss. 244(1),	OR/SR[37] OR SR (by disinterested members) SR (by disinterested members)	s. 76C (off market acquisition on equal access scheme) s. 76D(2) (selective off market acquisition) s.76DA(1)(contingent purchase contract) s. 76E(1) (market acquisition) (Cap 50)	OR SR (by disinterested members) SR OR	s. 68(2)(b) (India Companies Act 2013)	SR	s. 127(1)[38] (Act 777) LR 12.03-12.04 (market purchase) (Main Market Listing Requirements of Bursa Malaysia)	May purchase its own shares if authorized by the constitution ………OR	s. 694(2) (off market purchase) s. 701(1) (market purchase)	OR (by disinterested members) OR

33 s. 62(1)(a) suggests that shareholder approval is not required if it is a rights issue i.e. existing shareholders acquire new shares in proportion, as nearly as circumstances admit, to the paid-up share capital on those shares they held

34 Rule 804 provides that the directors issuing the shares and his/her associates shall not vote

35 Rules 806(2)(a) provides that if shareholders approve the mandate by ordinary resolution, the limit must be not more than 100% of the total number of issued shares excluding treasury shares, of which the aggregate number of shares and convertible securities issued other than on a pro rata basis to existing shareholders must be not more than 50% of the total number of issued shares excluding treasury shares

36 Rule 806(2)(b) provides that if shareholders approve the mandate by special resolution, the limit on the aggregate number of shares and convertible securities issued, whether on a pro rata or non pro rata basis, may be up to 100% of the total number of issued shares excluding treasury shares. Shareholder approval under this Rule 806(2)(b) must not be deemed by way of subscription for shares.

37 S. 238(3) provides that if under the proposed general offer, a member of the company may be compelled to dispose of the member's shares, the resolution authorising the offer must be a special resolution on which no non-tendering member votes

38 Only listed companies are allowed to purchase its own shares if so authorised by its constitution.

	246(1) (unlisted company buy-back shares under contract) (Cap 622)									
Financial assistance	s. 284(1)(c) s. 285(1)(d)	Approved by written resolution of all members of the company OR	s. 76(9B)(e) s. 76(10)(a) (Cap 50)	Resolution by all the members of the company[39] SR	s. 67(3(b) (India Companies Act 2013)	SR[40]	s. 126(2)[41] (Act 777)	SR[42]	/	/
Alteration of class rights attached to shares	s. 180(3) (Cap 622)	SR (of holders of shares in the class)[43]	s. 74(1) (Cap 50)	Provision is made by the constitution for authorising the variation or abrogation of the rights attached to any class of shares in the company, subject to the consent of any specified proportion of the holders of the issued shares of that class or the sanction of a resolution passed at a separate meeting of the holders of those shares	s. 48(1) (India Companies Act 2013)	SR (of holders of the issued shares of that class)[44]	s. 91 (Act 777)	SR[45]	s. 630(4)(b) (Companies Act 2006)	SR[46]

39 S. 76(9B)(e) provides that a resolution should be passed either by all the members of the company present and voting either in person or by proxy at the relevant meeting; or if the resolution is proposed to be passed by written means under section 184A, by all the members of the company, to give that assistance

40 Financial assistance can be given if it is in accordance with any scheme approved by company through special resolution and in accordance with such requirements as may be prescribed, for the purchase of, or subscription for, fully paid-up shares in the company or its holding company, if the purchase of, or the subscription for, the shares held by trustees is for the benefit of the employees or such shares held by the employee of the company

41 S. 126(1) provides that the exception to giving financial assistance does not apply to listed companies

42 The aggregate amount of the assistance and any other financial assistance given under this section that has not been repaid does not exceed 10% of the aggregate amount received by the company in respect of the issue of the shares and the reserves of the company, as such aggregate amount is disclosed in the most recent audited financial statements of the company

43 Alternatively, the rights can be varied with written consent of holders representing at least 75% of the total voting rights of holders of shares in the class

44 Alternatively, the rights attached to the shares of any class may be varied with the consent in writing of the holders of not less than three-fourths of the issued shares of that class

45 Alternatively, a written consent representing not less than 75% of the total voting rights of the shareholders in the class suffices.

46 Alternatively, consent to the variation of class rights may be given in writing from the holders of at least three-quarters in nominal value of the issued shares of that class (s.630(4)(a))

Appointment of Company's auditor	s. 396(1) (Cap 622)	OR	s. 205 (Cap 50)	OR[47]/SR[48]	s. 139(1) (India Companies Act 2013)	OR	s. 271(4) (Act 777)	OR	s. 489(4) (Companies Act 2006)	OR
Approving property transactions between director and company	s. 503(2)(a) and (3) [49] (Cap 622) LR 14A.36 (Listing Rules of the Stock Exchange of Hong Kong)	OR (by disinterested members)	s 162-163[50] (Cap 50) LR 906, LR 918 LR 919 (SGX-ST Listing Manual)	OR (by disinterested members) s.163(1) (Cap 50)	s. 188(1) (India Companies Act 2013)	OR (by disinterested members) Provided that no contract or arrangement, in the case of a company having a paid-up share capital of not less than such amount, or transactions exceeding such sums, as may be prescribed, shall be entered into except with the prior approval of the company by a resolution	s.228(1)(A)and (1)(B) (Act 777)	OR (by disinterested members)	s. 190(1) (Companies Act 2006)	OR
Winding Up	s. 228(1) (Cap 32)	OR[51] SR	s. 290 (Cap 50)	OR[52] SR	s. 59(3)(c) (The Insolvency and Bankruptcy Code 2016)	OR[53] SR	s. 439(1) (Act 777)	OR[54] s.439(1)(a) SR s.439(1)(b)	s. 84(1) (Insolvency Act 1986)	OR[55] (ss.1a) SR (ss. 1b)
Derivative Actions	s. 732 (Cap 622)	/	s. 216A (Cap 50)	/	Common Law[56]	/	s. 345(a) complainant includes member of		s. 260 (Companies Act 2006)	/

47 S. 205(2) provides that a company shall at each annual general meeting of the company appoint an accounting entity or accounting entities to be the auditor or auditors of the company, and any auditor or auditors so appointed shall, subject to this section, hold office until the conclusion of the next annual general meeting of the company. S. 205(7)(b) provides that where an auditor of a company is removed from office by resolution with special notice at a general meeting, the meeting may be adjourned to a date not earlier than 20 days and not later than 30 days after the meeting and the company may, by ordinary resolution, appoint another accounting entity as auditor, being an accounting entity notice of whose nomination as auditor has, at least 10 days before the resumption of the adjourned meeting, been received by the company.

48 S. 205(7)(a) provides that where an auditor of a company is removed from office by resolution with special notice at a general meeting, the company may, at the meeting, by a resolution passed by a majority of not less than three-fourths of such members of the company as being entitled to do so vote in person or, where proxies are allowed, by proxy immediately appoint another accounting entity nominated at the meeting as auditor

49 On credit transaction i.e. selling land to directors under a conditional sale agreement

50 On credit transaction i.e supplying or disposing immovable property to directors under a hire-purchase agreement or conditional sale agreement

51 s. 228(1)(a) provides that when the period, if any, fixed for the duration of the company by the articles expires, or the event, if any, occurs on the occurrence of which the articles provide that the company is to be dissolved, an OR is sufficient to dissolve the company

52 s.290(1)(a) provides that when the period, if any, fixed for the duration of the company by the constitution expires or the event, if any, happens, on the occurrence of which the constitution provides that the company is to be dissolved, an OR is sufficient to dissolve the company

53 s. 59(3)(c)(ii) provides that when the period of its duration, if any, fixed by its articles expires or on the occurrence of any event in respect of which the articles provide that the company shall be dissolved, an OR is sufficient to dissolve the company

54 s. 439(1)(a) provides that when the period, if any, fixed for the duration of the company by the constitution expires or the event, if any, happens, on the occurrence of which the constitution provides that the company is to be dissolved, an OR is sufficient to dissolve the company

55 s. 84(1)(a) provides that when the period (if any) fixed for the duration of the company by the articles expires, or the event (if any) occurs, on the occurrence of which the articles provide that the company is to be dissolved, an OR is sufficient to dissolve the company

56 *Nirad Amilal Mehta v. Genelec Ltd* [2008] 146 Comp. Cas. 481

							the company s. 347 (Act 777)			
Unfair Prejudice/ Oppression	s. 724 (Cap 622)	/	s. 216 (Cap 50) in cases of oppression or injustice	/	s. 245 (India Companies Act 2013)	/	s. 346(1) (Act 777)	/	s. 994 (Companies Act 2006)	/

Table 2: Top 30 listed companies in Hong Kong, Singapore, India and Malaysia

	Company Name
Hong Kong	
1.	Tencent Holdings Ltd.
2.	China Mobile Ltd.
3.	China Construction Bank Corporation - H Shares
4.	HSBC Holdings Plc
5.	AIA Group Ltd
6.	Industrial and Commercial Bank of China Ltd – H Shares
7.	Prudential Plc.
8.	CNOOC Ltd.
9.	Glencore Plc.
10.	CK Hutchison Holdings Ltd
11.	BOC (Hong Kong) Holdings Ltd.
12.	Bank of China Ltd. - H Shares
13.	Sun Hung Kai Properties Ltd
14.	CITIC Ltd.
15.	Ping An Insurance (Group) Co. of China, Ltd – H Shares
16.	Hang Seng Bank Ltd.
17.	Sands China Ltd.
18.	Manualife Financial Corporation
19.	China Overseas Land & Investment Ltd.
20.	MTR Corporation Ltd.
21.	Hong Kong Exchanges and Clearing Ltd.
22.	Standard Chartered PLC
23.	China Unicom (Hong Kong) Ltd.
24.	Bank of Communications Co., Ltd. – H Shares
25.	The Wharf (Holdings) Ltd.
26.	Cheung Kong Property Holdings Ltd.
27.	CLP Holdings Ltd.
28.	The Hong Kong and China Gas Co. Ltd.
29.	China Life Insurance Co. Ltd. – H Shares
30.	Galaxy Entertainment Group Ltd.
Singapore	
31.	Prudential PLC

	Company Name
32.	Singapore Telecommunications Limited
33.	DBS Group Holdings Ltd
34.	Oversea-Chinese Banking Corporation Limited
35.	United Overseas Bank
36.	Jardine Strategic Holdings Limited
37.	Jardine Matheson Holdings Limited
38.	Hongkong Land Holdings Limited
39.	Thai Beverage Public Company Limited
40.	Wilmar International Limited
41.	Jardine Cycle & Carriage Limited
42.	Dairy Farm International Holdings Limited
43.	CapitaLand Limited
44.	IHH Healthcare Berhad
45.	Global Logistic Properties Limited
46.	Genting Singapore PLC
47.	Keppel Corporation Limited
48.	Singapore Airlines Limited
49.	Singapore Technologies Engineering Ltd
50.	Great Eastern Holdings Limited
51.	City Developments Limited
52.	Singapore Exchange Limited
53.	Shangri-La Asia Limited
54.	Ascendas Real Estate Investment Trust
55.	CapitaLand Mall Trust
56.	AusNet Services Ltd
57.	Alibaba Pictures Group Limited
58.	UOL Group Limited
59.	ComfortDelGro Corporation Limited
60.	Sembcorp Industries Ltd
India	
61.	Tata Consultancy Services Limited
62.	Reliance Industries Ltd
63.	HDFC Bank Ltd
64.	ITC Ltd
65.	State Bank of India
66.	Housing Development Finance Corporation Ltd
67.	Oil and Natural Gas Corporation Ltd

	Company Name
68.	Infosys Ltd
69.	Hindustan Unilever Ltd
70.	Indian Oil Corporation
71.	Maruti Suzuki India Ltd
72.	ICICI Bank Ltd
73.	Kotak Mahindra Bank Ltd
74.	Coal India Ltd
75.	Larsen & Toubro Ltd
76.	Sun Pharmaceutical Industries Ltd
77.	Bharti Airtel Ltd
78.	NTPC Ltd
79.	Tata Motors Ltd
80.	Wipro Ltd
81.	HCL Technologies Limited
82.	Axis Bank Ltd
83.	Ultratech Cement Ltd
84.	Power Grid Corporation of India Ltd
85.	Asian Paints Ltd
86.	Hindustan Zinc Ltd
87.	Bharat Petroleum Corporation Ltd
88.	Bajaj Auto Ltd
89.	Mahindra & Mahindra Ltd
90.	Indusind Bank Ltd
Malaysia	
91.	Public Bank BHD
92.	Tenaga Nasional
93.	Malayan Banking
94.	Sime Darby Bhd
95.	CIMB Group Holdings
96.	Axiata Group Bhd
97.	Petronas Chemicals Group Bhd
98.	Digi.com
99.	IHH Healthcare
100.	Genting
101.	Petronas Gas
102.	Maxis Bhd
103.	IOI
104.	Telekom Malaysia
105.	Genting Malaysia BHD
106.	Kuala Lumpur Kepong
107.	MISC
108.	IJM
109.	PPB Group
110.	Hong Leong Bank

	Company Name
111.	AMMB Holdings
112.	YTL Corp
113.	Petronas Dagangan Bhd
114.	British American Tobacco (Malaysia)
115.	Astro Malaysia Holdings
116.	RHB Bank
117.	Westports Holdings
118.	Hap Seng Consolidated
119.	KLCC Prop&Reits-Stapled Sec
120.	Hong Leong Financial

Table 3: Materials collected from the top 30 listed companies

	Company	Annual Report	Website	Mission Statement	CSR/ESG Reports
Hong Kong					
1.	Tencent Holdings Ltd.	2015 2014	X	X	
2.	China Mobile Ltd.	2015 2014	X		2015 CSR Report 2014 CSR Report
3.	China Construction Bank Corporation - H Shares	2015 2014	X	X	
4.	HSBC Holdings Plc	2016 2015	X	X	
5.	AIA Group Ltd	2016 2015	X	X	2016 ESG Report 2015 CSR Report
6.	Industrial and Commercial Bank of China Ltd – H Shares	2015 2014	X	X	2016 CSR Report 2015 CSR Report
7.	Prudential Plc.	2015 2014	X	X	
8.	CNOOC Ltd.	2015 2014	X		2015 Social Responsibility Report 2014 Social Responsibility Report
9.	Glencore Plc.	2016 2015	X	X	2015 Sustainability Report 2014 Sustainability Report
10.	CK Hutchison Holdings Ltd	2015 2014	X		2015 ESG Report 2014 ESG Report
11.	BOC (Hong Kong) Holdings Ltd.	2015 2014	X	X	2015 CSR Report 2014 CSR Report

	Company	Annual Report	Website	Mission Statement	CSR/ESG Reports
12.	Bank of China Ltd. - H Shares	2015 2014	X	X	2015 CSR Report 2014 CSR Report
13.	Sun Hung Kai Properties Ltd	2015 2014	X	X	2015/16 Sustainability Report 2014/15 Sustainability Report
14.	CITIC Ltd.	2015 2014	X		
15.	Ping An Insurance (Group) Co. of China, Ltd – H Shares	2015 2014	X	X	2016 CSR Report
16.	Hang Seng Bank Ltd.	2016 2015	X		2015 CSR Report 2014 CSR Report
17.	Sands China Ltd.	2015 2014	X	X	
18.	Manualife Financial Corporation	2016 2015	X	X	
19.	China Overseas Land & Investment Ltd.	2015 2014	X	X	2015 ESG Report 2014 CSR Report
20.	MTR Corporation Ltd.	2015 2014	X		2015 Sustainability Report 2014 Sustainability Report
21.	Hong Kong Exchanges and Clearing Ltd.	2016 2015	X	X	2016 CSR Report 2015 CSR Report
22.	Standard Chartered PLC	2016 2015 2013	X	X	2016 Sustainability Summary 2015 Sustainability Summary 2013 Sustainability Review
23.	China Unicom (Hong Kong) Ltd.	2015 2014	X		

	Company	Annual Report	Website	Mission Statement	CSR/ESG Reports
24.	Bank of Communications Co., Ltd. – H Shares	2015 2014	X		2015 CSR Report 2014 CSR Report
25.	The Wharf (Holdings) Ltd.	2015 2014	X		2015 CSR Report 2014 CSR Report
26.	Cheung Kong Property Holdings Ltd.	2015	X		
27.	CLP Holdings Ltd.	2016 2015	X	X	2016 Sustainability Report 2015 Sustainability Report
28.	The Hong Kong and China Gas Co. Ltd.	2015 2014	X	X	2015 Sustainability Report 2014 Sustainability Report
29.	China Life Insurance Co. Ltd. – H Shares	2015 2014	X	X	2016 CSR Report 2015 CSR Report
30.	Galaxy Entertainment Group Ltd.	2016 2015	X	X	
Singapore					
31.	Prudential PLC	2016 2015	X	X	2016 ESG Report
32.	Singapore Telecommunications Limited	2016 2015	X	X	2016 Group Sustainability Report 2015 Group Sustainability Report
33.	DBS Group Holdings Ltd	2016 2015	X	X	
34.	Oversea-Chinese Banking Corporation Limited	2016 2015	X	X	
35.	United Overseas Bank	2016 2015	X	X	
36.	Jardine Strategic Holdings Limited	2016 2015			
37.	Jardine Matheson Holdings Limited	2016	X		

	Company	Annual Report	Website	Mission Statement	CSR/ESG Reports
38.	Hongkong Land Holdings Limited	2016 2015	X		2016 Sustainability Report 2015 Sustainability Report
39.	Thai Beverage Public Company Limited	2016 2015	X	X	2016 Sustainability Report 2015 Sustainability Report
40.	Wilmar International Limited	2016 2015	X		2015 Sustainability Report 2013 Sustainability Report
41.	Jardine Cycle & Carriage Limited	2016	X		
42.	Dairy Farm International Holdings Limited	2016 2015	X	X	
43.	CapitaLand Limited	2016 2015	X		2015 Global Sustainability Report 2014 Global Sustainability Report
44.	IHH Healthcare Berhad	2015 2014	X	X	
45.	Global Logistic Properties Limited	2016 2015	X	X	
46.	Genting Singapore PLC	2016 2015	X	X	2015 Sustainability Report
47.	Keppel Corporation Limited	2016 2015	X	X	2015 Sustainability Report 2014 Sustainability Report
48.	Singapore Airlines Limited	2016 2015	X	X	2015/2016 Sustainability Report 2014/2015 Sustainability Report

	Company	Annual Report	Website	Mission Statement	CSR/ESG Reports
49.	Singapore Technologies Engineering Ltd	2016 2015	X	X	2015 Risk and Sustainability Report 2014 Sustainability Report
50.	Great Eastern Holdings Limited	2016 2015	X	X	
51.	City Developments Limited	2016 2015	X	X	2016 Integrated Sustainability Report 2015 Sustainability Report
52.	Singapore Exchange Limited	2016 2015	X	X	2016 Sustainability Report 2015 Sustainability Report
53.	Shangri-La Asia Limited	2016 2015	X	X	2016 ESG Report 2015 ESG Report
54.	Ascendas Real Estate Investment Trust	2016 2015	X	X	2016 Sustainability Report 2015 Sustainability Report
55.	CapitaLand Mall Trust	2016 2015	X	X	
56.	AusNet Services Ltd	2016 2015	X	X	
57.	Alibaba Pictures Group Limited	2016 2015			
58.	UOL Group Limited	2016 2015	X	X	2015 Sustainability Report 2014 Sustainability Report
59.	ComfortDelGro Corporation Limited	2016 2015	X	X	2016 Sustainability Report

	Company	Annual Report	Website	Mission Statement	CSR/ESG Reports
					2015 Sustainability Report
60.	Sembcorp Industries Ltd	2016 2015	X	X	2016 ESG Review 2015 Sustainability Report
India					
61.	Tata Consultancy Services Limited	2016-2017 2015-2016	X	X	2015-2016 Corporate Sustainability Report 2014-2015 Corporate Sustainability Report
62.	Reliance Industries Ltd	2015-2016 2014-2015	X	X	2015-2016 Sustainability Report 2014-2015 Sustainability Report
63.	HDFC Bank Ltd	2015-2016 2014-2015	X	X	2015-2016 Annual Business Responsibility Report 2014-2015 Annual Business Responsibility Report
64.	ITC Ltd	2015-2016 2014-2015	X	X	2016 Sustainability Report 2015 Sustainability Report
65.	State Bank of India	2015-2016 2014-2015	X	X	2015-2016 Sustainability Report
66.	Housing Development Finance Corporation Ltd	2015-2016 2014-2015	X	X	2014-2015 Business Responsibility Report 2015-2016 Business

	Company	Annual Report	Website	Mission Statement	CSR/ESG Reports
					Responsibility Report
67.	Oil and Natural Gas Corporation Ltd	2015-2016 2014-2015	X	X	2016 Sustainability Report 2015 Sustainability Report
68.	Infosys Ltd	2015-2016 2014-2015	X		2015-2016 Sustainability Report 2014-2015 Sustainability Report
69.	Hindustan Unilever Ltd	2015-2016 2014-2015	X	X	2015-2016 Business Responsibility Report 2014-2015 Business Responsibility Report
70.	Indian Oil Corporation	2015-2016 2014-2015	X	X	2015-2016 Sustainability Report 2014-2015 Sustainability Report
71.	Maruti Suzuki India Ltd	2015-2016 2014-2015	X	X	2015-2016 Sustainability Report 2014-2015 Sustainability Report
72.	ICICI Bank Ltd	2016-2017 2015-2016	X		2016-2017 Business Responsibility Report 2015-2016 Business Responsibility Report
73.	Kotak Mahindra Bank Ltd	2015-2016 2014-2015	X	X	2016 Business Responsibility Report 2015 Business Responsibility Report

	Company	Annual Report	Website	Mission Statement	CSR/ESG Reports
74.	Coal India Ltd	2015-2016 2014-2015	X	X	2015-2016 Sustainability Report 2014-2015 Sustainability Report
75.	Larsen & Toubro Ltd	2015-2016 2014-2015	X		2016 Sustainability Report
76.	Sun Pharmaceutical Industries Ltd	2015-2016 2014-2015	X		2015-2016 Business Responsibility Report 2014-2015 Business Responsibility Report
77.	Bharti Airtel Ltd	2015-2016 2014-2015	X	X	2016 Sustainability Report 2015 Sustainability Report
78.	NTPC Ltd	2015-2016 2014-2015	X	X	2014-2015 & 2015-2016 Sustainability Report
79.	Tata Motors Ltd	2015-2016 2014-2015	X	X	2015-2016 Sustainability Report 2014-2015 Sustainability Report
80.	Wipro Ltd	2015-2016 2014-2015	X		2014-2015 Sustainability Report 2013-2014 Sustainability Report
81.	HCL Technologies Limited	2015-2016 2014-2015	X		2016 Sustainability Report 2015 Sustainability Report
82.	Axis Bank Ltd	2015-2016	X		2014-2015 Sustainability Report

	Company	Annual Report	Website	Mission Statement	CSR/ESG Reports
					2015-2016 Sustainability Report
83.	Ultratech Cement Ltd	2015-2016 2014-2015	X		2015 Sustainability Report 2014 Sustainability Report
84.	Power Grid Corporation of India Ltd	2015-2016 2014-2015	X	X	2015-2016 CSR Annual Booklet 2014-2015 CSR Annual Booklet
85.	Asian Paints Ltd	2015-2016 2014-2015	X		2015-2016 Sustainability Report 2014-2015 Sustainability Report
86.	Hindustan Zinc Ltd	2015-2016 2014-2015	X	X	2015-2016 Sustainability Report
87.	Bharat Petroleum Corporation Ltd	2015-2016 2014-2015	X	X	2015-2016 Sustainability Report 2014-2015 Sustainability Report
88.	Bajaj Auto Ltd	2015-2016 2014-2015	X		Annexure to the Annual Report on CSR activities for the year ended 31 March 2016 Annexure to the Annual Report on CSR activities for the year ended 31 March 2015
89.	Mahindra & Mahindra Ltd	2015-2016 2014-2015	X	X	2015-2016 Sustainability Report 2014-2015 Sustainability Report

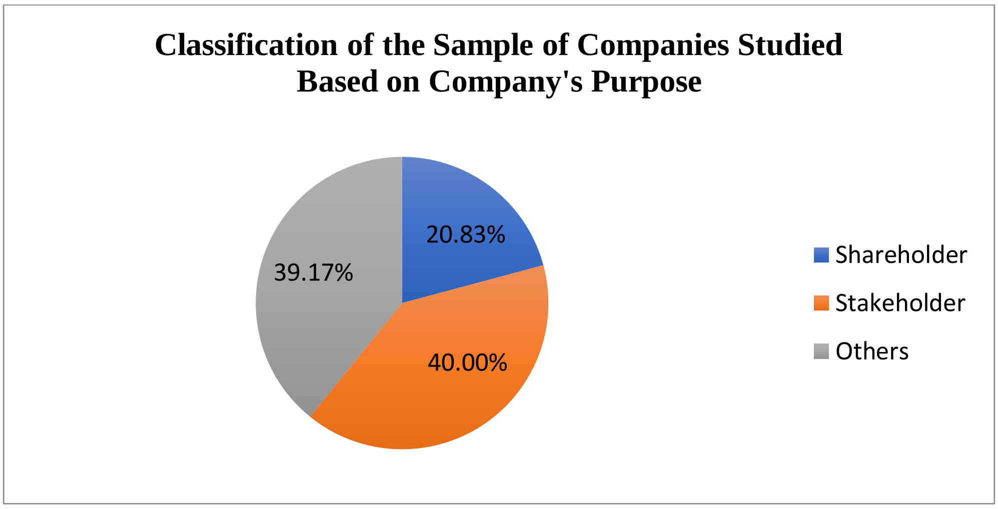
	Company	Annual Report	Website	Mission Statement	CSR/ESG Reports
90.	Indusind Bank Ltd	2015-2016 2014-2015	X	X	2015-2016 Sustainability Report 2014-2015 Sustainability Report
Malaysia					
91.	Public Bank BHD	2016 2015	X	X	
92.	Tenaga Nasional	2016 2015	X	X	
93.	Malayan Banking	2016 2015	X	X	2015 Sustainability Report 2014 Sustainability Report
94.	Sime Darby Bhd	2016 2015	X	X	
95.	CIMB Group Holdings	2016 2015	X	X	2016 Citizenship Report 2015 Sustainability Report
96.	Axiata Group Bhd	2016 2015	X	X	2016 Sustainability & National Contribution Report 2015 Sustainability & National Contribution Report
97.	Petronas Chemicals Group Bhd	2016 2015	X		
98.	Digi.com	2016 2015	X		2016 Sustainability Report 2015 Sustainability Report
99.	IHH Healthcare	2015 2014	X	X	
100.	Genting	2016 2015	X	X	2016 Sustainability Report

	Company	Annual Report	Website	Mission Statement	CSR/ESG Reports
					2015 Sustainability Report
101.	Petronas Gas	2016 2015	X	X	2016 Sustainability Report 2015 Sustainability Report
102.	Maxis Bhd	2016 2015	X		2016 Sustainability Report 2015 Sustainability Report
103.	IOI	2016 2015	X		
104.	Telekom Malaysia	2016 2015	X	X	2016 Sustainability Report 2015 Sustainability Report
105.	Genting Malaysia BHD	2016 2015	X	X	2016 Sustainability Report 2015 Sustainability Report
106.	Kuala Lumpur Kepong	2016 2015	X	X	2016 Sustainability Report
107.	MISC	2016 2015	X	X	2015 Sustainability Report
108.	IJM	2016 2015	X	X	
109.	PPB Group	2016 2015	X	X	
110.	Hong Leong Bank	2016 2015	X		
111.	AMMB Holdings	2016 2015	X	X	
112.	YTL Corp	2016 2015	X		2016 Sustainability Report

	Company	Annual Report	Website	Mission Statement	CSR/ESG Reports
					2015 Sustainability Report
113.	Petronas Dagangan Bhd	2016 2015	X	X	2016 Sustainability Report 2015 Sustainability Report
114.	British American Tobacco (Malaysia)	2016 2015	X		2016 Sustainability Summary Report 2015 Sustainability Summary Report
115.	Astro Malaysia Holdings	2017 2016	X		
116.	RHB Bank	2016 2015	X	X	
117.	Westports Holdings	2016 2015	X	X	2016 Sustainability Report
118.	Hap Seng Consolidated	2016 2015	X	X	
119.	KLCC Prop&Reits-Stapled Sec	2016 2015	X	X	2016 Sustainability Statement 2015 Corporate Responsibility and Sustainability Report
120.	Hong Leong Financial	2016	X		2014 Sustainability Report

Table 4: Classification of the top 30 listed companies based on company's purpose

(i) Overview



Shareholder	Stakeholder	Others
Ascendas Real Estate Investment Trust	AMMB Holdings	AIA Group Ltd.
Astro Malaysia Holdings	AusNet Services Ltd	Alibaba Pictures Group Limited
British American Tobacco (Malaysia)	Axiata Group Bhd	Asian Paints Ltd
CapitaLand Mall Trust	Bharat Petroleum Corporation Ltd	Axis Bank Ltd
Cheung Kong Property Holdings Ltd.	Bharti Airtel Ltd	Bajaj Auto Ltd
China Mobile Ltd.	BOC (Hong Kong) Holdings Ltd.	Bank of China Ltd. - H Shares
China Unicom (Hong Kong) Ltd.	China Construction Bank Corporation – H Shares	Bank of Communications Co., Ltd. – H Shares
CITIC Ltd.	China Overseas Land & Investment Ltd.	CapitaLand Limited

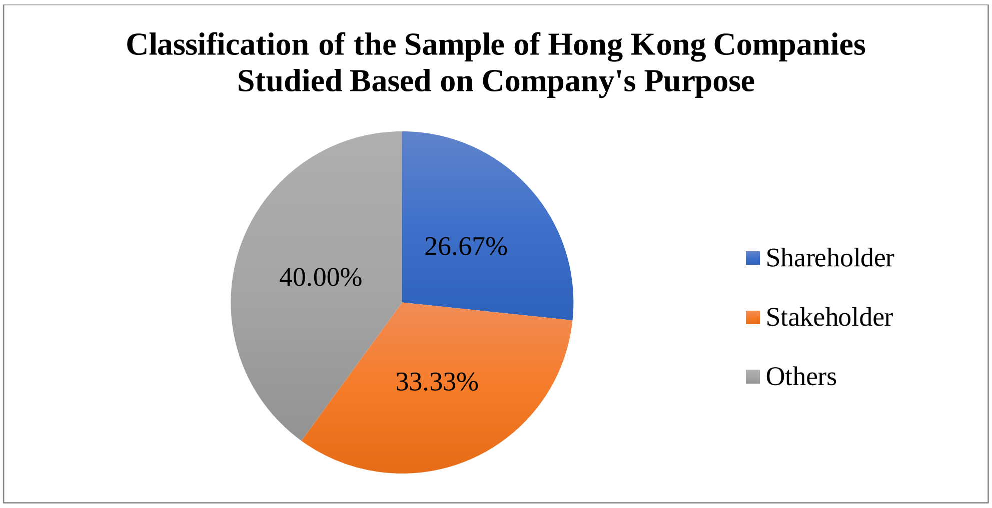
Shareholder	**Stakeholder**	**Others**
CK Hutchison Holdings Ltd	CLP Holdings Ltd.	China Life Insurance Co.
Digi.com	Dairy Farm International Holdings Limited	CIMB Group Holdings
Glencore Plc	Genting	City Developments Limited
Jardine Cycle & Carriage Limited	Genting Malaysia BHD	CNOOC Ltd.
Jardine Matheson Holdings Limited	Great Eastern Holdings Limited	Coal India Ltd
KLCC Prop&Reits-Stapled Sec	Hap Seng Consolidated	ComfortDelGro Corporation Limited
Kotak Mahindra Bank Ltd	HCL Technologies Limited	DBS Group Holdings Ltd
Manualife Financial Corporation	Hindustan Zinc Ltd	Galaxy Entertainment Group Ltd.
Oversea-Chinese Banking Corporation Limited	Hong Leong Bank	Genting Singapore PLC
Petronas Chemicals Group Bhd	Hong Leong Financial	Global Logistic Properties Limited
Petronas Dagangan Bhd	IHH Healthcare	Hang Seng Bank Ltd.
Petronas Gas	IHH Healthcare Berhad	HDFC Bank Ltd
Singapore Telecommunications Limited	IJM	Hindustan Unilever Ltd

Shareholder	**Stakeholder**	**Others**
Standard Chartered PLC	Industrial and Commercial Bank of China Ltd – H Shares	Hong Kong Exchanges and Clearing Ltd.
Sun Pharmaceutical Industries Ltd	Infosys Ltd	Hongkong Land Holdings Limited
Tenaga Nasional	Keppel Corporation Limited	Housing Development Finance Corporation Ltd
YTL Corp	Larsen & Toubro Ltd	HSBC Holdings Plc
	Mahindra & Mahindra Ltd	ICICI Bank
	Malayan Banking	Indian Oil Corporation
	Maxis Bhd	Indusind Bank Ltd
	NTPC Ltd	IOI
	Prudential PLC	ITC Ltd
	Prudential Plc.	Jardine Strategic Holdings Limited
	Reliance Industries Ltd	Kuala Lumpur Kepong
	Shangri-La Asia Limited	Maruti Suzuki India Ltd
	Sime Darby Bhd	MISC
	Singapore Airlines Limited	MTR Corporation Ltd.
	State Bank of India	Oil and Natural Gas Corporation
	Sun Hung Kai Properties Ltd	Ping An Insurance (Group) Co. of China, Ltd – H Shares

Shareholder	Stakeholder	Others
	Tata Consultancy Services Limited	Power Grid Corporation of India Ltd
	Tata Motors Ltd	PPB Group
	Tencent Holdings Ltd.	Public Bank BHD
	Thai Beverage Public Company Limited	RHB Bank
	The Hong Kong and China Gas Co. Ltd.	Sands China Ltd.
	The Wharf (Holdings) Ltd.	Singapore Exchange Limited
	Ultratech Cement Ltd	Sembcorp Industries Ltd
	United Overseas Bank	Singapore Technologies Engineering Ltd
	UOL Group Limited	Telekom Malaysia
	Westports Holdings	Wilmar International Limited
	Wipro Ltd	

(ii) By Jurisdiction

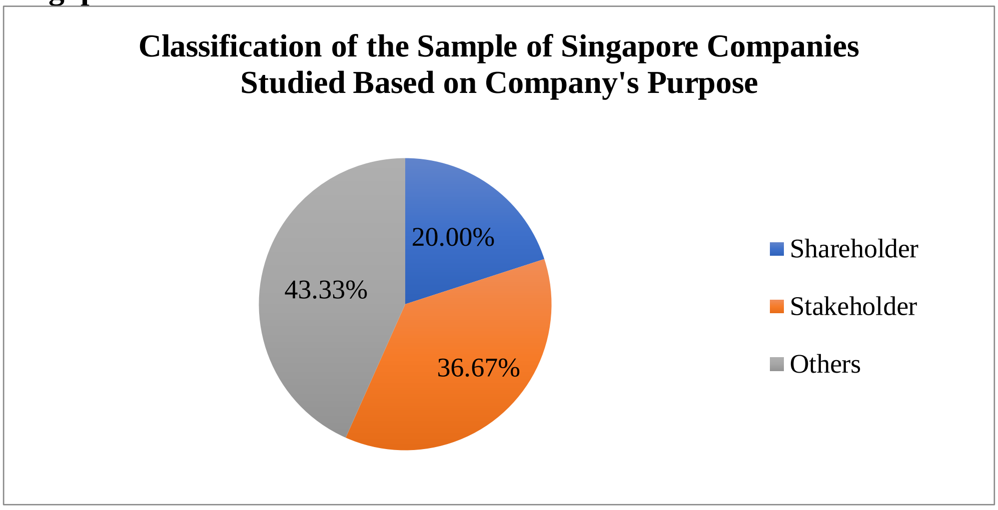
a. Hong Kong



Shareholder	Stakeholder	Others
Cheung Kong Property Holdings Ltd.	BOC (Hong Kong) Holdings Ltd.	AIA Group Ltd.
China Mobile Ltd.	China Construction Bank Corporation – H Shares	Bank of China Ltd. - H Shares
China Unicom (Hong Kong) Ltd.	China Overseas Land & Investment Ltd.	Bank of Communications Co., Ltd. – H Shares
CK Hutchison Holdings Ltd	CLP Holdings Ltd.	China Life Insurance Co.
CITIC Ltd.	Industrial and Commercial Bank of China Ltd – H Shares	CNOOC Ltd.
Glencore Plc	Sun Hung Kai Properties Ltd	Galaxy Entertainment Group Ltd.
Manualife Financial Corporation	Tencent Holdings Ltd.	Hang Seng Bank Ltd.
Standard Chartered PLC	The Hong Kong and China Gas Co. Ltd.	Hong Kong Exchanges and Clearing Ltd.
	The Wharf (Holdings) Ltd.	HSBC Holdings Plc
	Prudential Plc.	MTR Corporation Ltd.

Shareholder	Stakeholder	Others
		Ping An Insurance (Group) Co. of China, Ltd – H Shares
		Sands China Ltd.

b. Singapore

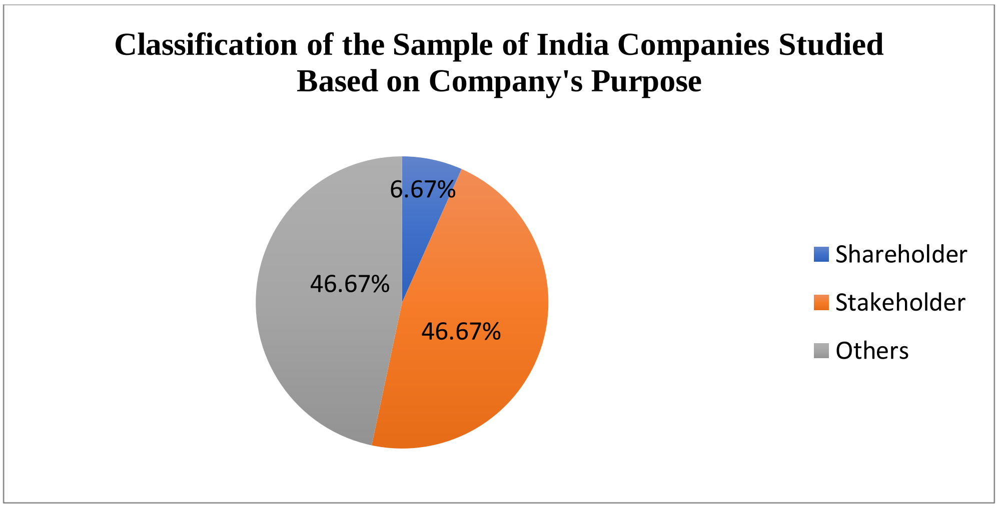


Classification of the Sample of Singapore Companies Studied Based on Company's Purpose

Shareholder	Stakeholder	Others
Ascendas Real Estate Investment Trust	AusNet Services Ltd	Alibaba Pictures Group Limited
CapitaLand Mall Trust	Dairy Farm International Holdings Limited	CapitaLand Limited
Oversea-Chinese Banking Corporation Limited	Great Eastern Holdings Limited	City Developments Limited
Singapore Telecommunications Limited	IHH Healthcare Berhad	ComfortDelGro Corporation Limited
Jardine Matheson Holdings Limited	Keppel Corporation Limited	DBS Group Holdings Ltd
Jardine Cycle & Carriage Limited	Prudential PLC	Genting Singapore PLC
	Shangri-La Asia Limited	Global Logistic Properties Limited
	Singapore Airlines Limited	Hongkong Land Holdings Limited

Shareholder	**Stakeholder**	**Others**
	Thai Beverage Public Company Limited	Jardine Strategic Holdings Limited
	United Overseas Bank	Singapore Exchange Limited
	UOL Group Limited	Sembcorp Industries Ltd
		Singapore Technologies Engineering Ltd
		Wilmar International Limited

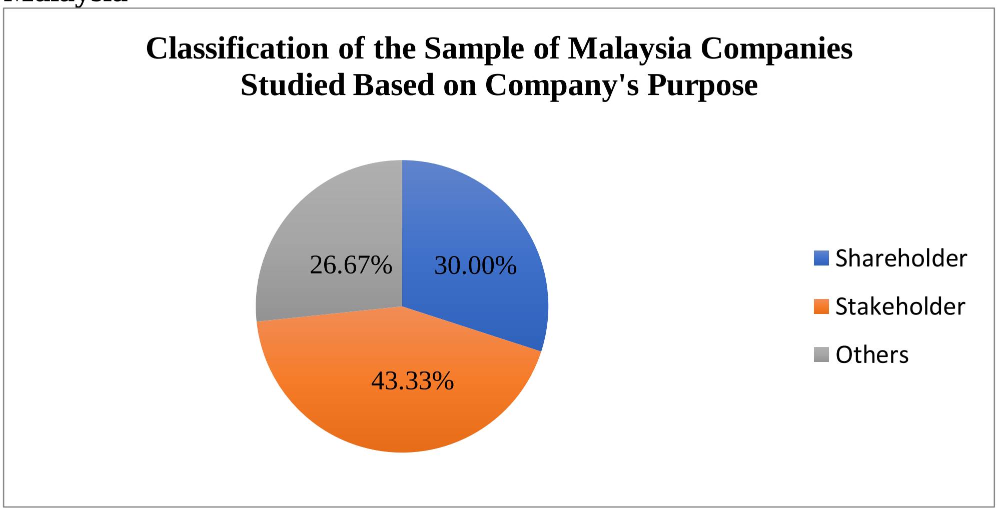
c. India



Shareholder	**Stakeholder**	**Others**
Kotak Mahindra Bank Ltd	Bharat Petroleum Corporation Ltd	Asian Paints Ltd
Sun Pharmaceutical Industries Ltd	Bharti Airtel Ltd	Axis Bank Ltd
	HCL Technologies Limited	Bajaj Auto Ltd
	Hindustan Zinc Ltd	Coal India Ltd
	Infosys Ltd	HDFC Bank Ltd
	Larsen & Toubro Ltd	Hindustan Unilever Ltd
	Mahindra & Mahindra Ltd	Housing Development Finance Corporation Ltd

Shareholder	Stakeholder	Others
	NTPC Ltd	ICICI Bank
	Reliance Industries Ltd	Indian Oil Corporation
	State Bank of India	Indusind Bank Ltd
	Tata Consultancy Services Limited	ITC Ltd
	Tata Motors Ltd	Maruti Suzuki India Ltd
	Ultratech Cement Ltd	Oil and Natural Gas Corporation
	Wipro Ltd	Power Grid Corporation of India Ltd

d. Malaysia



Shareholder	Stakeholder	Others
Astro Malaysia Holdings	AMMB Holdings	CIMB Group Holdings
British American Tobacco (Malaysia)	Axiata Group Bhd	IOI
Digi.com	Genting	Kuala Lumpur Kepong

Shareholder	**Stakeholder**	**Others**
KLCC Prop&Reits-Stapled Sec	Genting Malaysia BHD	MISC
Petronas Chemicals Group Bhd	Hap Seng Consolidated	PPB Group
Petronas Dagangan Bhd	Hong Leong Bank	Public Bank BHD
Petronas Gas	Hong Leong Financial	RHB Bank
Tenaga Nasional	IHH Healthcare	Telekom Malaysia
YTL Corp	IJM	
	Malayan Banking	
	Maxis Bhd	
	Sime Darby Bhd	
	Westports Holdings	

DPHIL CHAPTER 1: INTRODUCTION

I. The central argument[1]

This thesis seeks to reconceptualise the role of controlling shareholders as one that should include fiduciary duties. The case study consists of the listed companies in the four common law jurisdictions in Asia, namely, Hong Kong, Singapore, India and Malaysia. My central argument is that controlling shareholders in the listed companies in these common law jurisdictions in Asia should owe fiduciary duties to the company, consisting of the duty to act in good faith in the best interests of the company and the duty to avoid unauthorised conflict of interest and unauthorised receipt of profits. The term 'interests of the company' in the best interest duty could refer to the long-term value and viability of the company as a distinct and separate entity, whose interests are not equated with, or reducible to, those of shareholders (or any particular stakeholder).

[1] This thesis draws upon but is a substantially and significantly revised version of a prior published work, namely, Ernest Lim, 'Controlling Shareholders and Fiduciary Duties in Common Law Asia' (2018) 18 *Journal of Corporate Law Studies* 113.

II. The problem

The principles of company law in the common law jurisdictions in Asia - Singapore, Hong Kong, India and Malaysia - are based on or derived from English common law (despite differences in statutory law). However, the ownership structure of the listed companies of these common law systems in Asia is markedly different from that in the UK. While the UK is a dispersed ownership system, the common law Asian systems consist mainly of concentrated ownership, and the listed companies there are, and will continue to be, dominated by controlling shareholders comprising mainly families and the state.[2]

Different ownership structures pose different problems and therefore warrant different legal strategies. In a dispersed ownership jurisdiction such as the UK, the key problem is the separation of ownership and control where the directors and managers can misuse their powers to pursue their personal interests at the expense of the shareholders, or the directors can be negligent to the detriment of the company. By contrast, in a concentrated ownership jurisdiction, the key problem is 'tunneling'[3], which refers to the 'transfer of resources out of a company to its controlling shareholder', or more broadly speaking, extraction of 'private benefits of control'[4] by controlling shareholders where they acquire benefits that are not shared with the company and minority shareholders.[5] Such extractions of private benefits of control take place where there are conflicts of interest, and in a variety of contexts, including but not limited to

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[2] See Chapter 3.

[3] See eg, Vladimir Atanasov and others, 'Law and Tunnelling' (2011) 37 *Journal of Corporation Law* 1.

[4] Simon Johnson and others, 'Tunneling' (2000) 90 *American Economic Review* 22, 22.

[5] It does not follow that controlling shareholders or concentrated ownership companies are necessarily a bad thing: see Chapter 3.

self-dealing transactions between the controlling shareholder and the company. The extraction of private benefits of control is exacerbated by the presence of pyramid and cross-holding structures in many listed companies in common law Asia.[6] By virtue of their dominant powers, controlling shareholders could use the general meeting to perpetuate and legitimise their powers and to extract private benefits of control. Further, the already significant powers conferred on shareholders[7] are amplified when these shareholders are the controllers themselves. Thus, companies dominated by controlling shareholders in common law Asia are seldom vulnerable to the threat of takeover, an important disciplinary mechanism, as compared to those in the UK.

However, although the ownership structure and thus, the corporate governance problems in the UK are different from those in the former British colonies in Asia, the legal principles regulating the exercise of discretionary powers by directors, as well as those regulating conflicts of interest involving directors and shareholders, are substantially the same. One significant feature in both the UK and the common law jurisdictions in Asia is that duties are imposed only on directors, not shareholders. Notably, shareholders generally do not owe duties to the company (or minority shareholders). Another important legal principle that the common law Asian jurisdictions inherited from the UK is that shareholders are not subject to fiduciary duties because they can vote as they please and they are not agents of the company. But as mentioned earlier, conflicts of interest between controlling shareholders and the company, and thus extractions of private benefits of control, are a central and persistent issue in the common law systems in Asia[8], unlike the case in the UK.

[6] See Chapter 3.

[7] Ibid.

[8] Ibid.

Thus, the question, broadly framed, is what reforms ought to be made to a corporate law system (i.e. common law Asia) when it is based on, or derived from, another corporate law system (i.e. the UK), although both systems have different corporate governance problems. The specific issue is whether these common law jurisdictions in Asia should still adhere to the current UK company law position under which shareholders owe no duties, or whether they ought to subject controlling shareholders to fiduciary duties. I argue that these common law systems in Asia should subject the controlling shareholders of listed companies to fiduciary duties. In the next two sections, I elaborate on why I have selected the common law Asian jurisdictions for analysis and I explain the scope of fiduciary duties.

III. Why the common law Asian jurisdictions?

A. Common law Asia

I will first explain why I have selected the common law jurisdictions in Asia and then the four jurisdictions specifically for analysis. Common law Asia, despite its economic success, geopolitical importance and legal significance, has been neglected by many comparative corporate law scholars who have mainly focused on the Anglo-American and continental European jurisdictions. It is telling that none of the leading and established works on comparative company law and corporate governance contains any analysis of the common law jurisdictions in Asia (although Japan which is a civil law and dispersed ownership jurisdiction is sometimes covered, and recent and fleeting references are made to India).[9] Further, given that the majority of public companies outside of the UK and US are, and will continue to be, dominated by controlling shareholders[10], more attention should be paid to the problem of conflicts of interest and extractions of private benefits of control.[11]

Although the corporate laws of the common law jurisdictions in Asia are derived from or inspired by English law, there are significant differences between them and the UK; this makes the use of these common law systems in Asia as a case study interesting and valuable. First, as mentioned earlier, the majority of the listed companies in common law Asia are characterised by concentrated ownership and control where pyramid and cross-holding structures are prevalent; by contrast, the UK is a dispersed ownership jurisdiction with separation of ownership and control. Second, as mentioned before, a central corporate governance issue in common law Asia is the conflict of interest between controlling shareholders and the company, whereas in the UK, it is between dispersed shareholders and the board/management. Third, the means through which the controlling shareholders benefit themselves include tunneling, cronyism and nepotism, whereas in the UK, the means through which the board/management benefit themselves include shirking, empire building and excessive compensation. Fourth, the primary (but not the sole) mechanism to address conflicts

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[9] See eg, Klaus J Hopt, 'Comparative Company Law' in Mathias Reimann and Reinhard Zimmerman (eds), *The Oxford Handbook of Comparative Law* (OUP 2007); Reinier Kraakman and others, *The Anatomy of Corporate Law: A Comparative and Functional Approach* (3rd edn, OUP 2017); Andreas Cahn and David C Donald, *Comparative Company Law: Text and Cases on the Corporate Laws of Germany, the UK and the US* (CUP 2010); Andreas M Fleckner and Klaus J Hopt (eds), *Comparative Corporate Governance: A Functional and International Analysis* (CUP 2013) and Mathias Siems and David Campbell (eds), *Comparative Company Law: A Case-Based Approach* (Hart 2013). But there is a gradually increasing number of works that include the common law Asian jurisdictions, see Dan W Puchniak and others (eds), *The Derivative Action in Asia: A Comparative and Functional Approach* (CUP 2012); Dan W Puchniak and others (eds), *Independent Directors in Asia: A Historical, Contextual and Comparative Approach* (CUP 2017).

[10] Rafael La Porta and others, 'Corporate Ownership Around the World' (1999) 54 *Journal of Finance* 471; Randall Morck and others, 'Corporate Governance, Economic Entrenchment and Growth' (2005) 63 *Journal of Financial Economics* 215.

[11] For an overview of the legal mechanisms to address this problem, see Kraakman (n 9) 80-88.

of interest (between the controlling shareholder and the company) in common law Asia is the regulation of related party transactions, whereas in the UK, directors may be liable for breaches of duties and the company may be subject to takeover. Fifth, shareholders in the listed companies in common law Asia consist mainly of either families or the government (or entities connected to the government); by contrast, in the UK, foreign shareholders and institutional investors constitute a significant percentage. Finally, the quality of the enforcement mechanism varies within the common law countries in Asia (with Hong Kong and Singapore ranking higher than India and Malaysia); by contrast, the UK has a generally robust system of enforcement. For these reasons, the common law systems in Asia provide a valuable case study.

B. The four jurisdictions[12]

These four Asian jurisdictions share similar critical features, in that they are all former British colonies; they all have predominantly concentrated corporate ownership structures consisting predominantly of state- and family-owned companies; and extractions of private benefits of control by controlling shareholders are common in all four. But there are differences

[12] Myanmar, another common law jurisdiction, is excluded, because as compared to the other four common law jurisdictions, its corporate law and governance regime is at a nascent stage and there are insufficient legal materials in the English language to allow for any sophisticated and nuanced assessment. The Myanmar Companies Law 2017 (which was passed in December 2017) replaced the Myanmar Company Act 1914 <https://www.aseanbriefing.com/news/2017/12/11/myanmars-new-companies-law.html> accessed 1 December 2018. The Yangon Stock Exchange was only set up in 2015 and it is the world’s smallest stock exchange <https://www.bloomberg.com/news/articles/2017-02-21/world-s-tiniest-stock-exchange-hungers-for-forbidden-foreigners> accessed 1 December 2018.

in the laws and institutional contexts among the four Asian jurisdictions which will further illuminate the arguments advanced in this thesis. By way of illustration, consider two examples below, which will be elaborated in subsequent chapters.

First, the jurisdictional differences among the Asian jurisdictions can shed light on what the term 'interests of the company' means with respect to the controlling shareholder's fiduciary duty to act in good faith in the interests of the company. India has a statutory provision that recognises the distinct interests of the company and that corporate interest is not synonymous with shareholders' interests. Although Singapore and Malaysia have no such statutory provision, the courts there have recognised that the interests of the company are distinct from those of shareholders and the former could be preferred over the latter. But the legal position in Hong Kong is substantially similar to that in the UK which equates corporate interest with shareholders' interests.

Second, the jurisdictional differences can shed light on how the fiduciary duties could be enforced. India has a statutory class action law suit to facilitate private enforcement unlike the other three jurisdictions. Hong Kong has an effective public enforcement mechanism which allows the regulator to address harms done to the company or shareholders, unlike the other three countries. Moreover, the fact that the courts in Malaysia and India are considered less independent than those in Singapore and Hong Kong may have implications for claims made against the controlling shareholder who is the government.

IV. The scope of fiduciary duties[13]

The fiduciary duties that are analysed in this thesis consist of the duty to act in good faith in the best interests of the company and the duty to avoid unauthorised conflict of interest and unauthorised receipt of profits.[14] Regarding the best interest duty, it has been held to be the 'core'[15] or 'fundamental'[16] fiduciary duty (in the context of directors' duties).[17] Further, the

[13] There are debates related to the fiduciary duties that comprise the core content of loyalty and the nature of loyalty: see eg, Andrew S Gold and Paul B Miller (eds), *Philosophical Foundations of Fiduciary Law* (OUP 2014); and D Gordon Smith and Andrew S Gold (eds), *Research Handbook on Fiduciary Law* (Edward Elgar 2018). It is outside the aims and scope of this book to analyse these issues.

[14] Under English law and the laws of the four common law Asian jurisdictions, the duty to exercise care and skill is not a fiduciary duty: see *Bristol and West Building Society v Mothew* [1998] Ch 1, 18; *Colin Gwyer v London Wharf (Limehouse) Ltd* [2002] EWHC 2748 (Ch), [2003] 2 BCLC 153, [83]. An important implication with characterising a duty as fiduciary or non-fiduciary lies with the remedies that are available. A breach of the fiduciary duty to avoid unauthorised conflict of interest and receipt of profit attracts the remedy of disgorgement of profits, but not a breach of non-fiduciary duty. A breach of the duty to exercise care and skill only attracts common law damages, but if the breach of this duty is accompanied by a breach of the no-conflict and no-profit rule, it will also attract disgorgement of profits, and if both common law damages and disgorgement of profits are available, the claimant has to elect between them. Where there is a breach of the fiduciary duty to act in the company's best interests but there is no breach of the no-conflict and no-profit rule, equitable compensation but not disgorgement of profits will be available. But where there is both a breach of the best interest duty as well as the no-conflict and no-profit rule, both equitable compensation and disgorgement of profits would be available and the claimant has to elect between them: *Tang Man Sit v Capacious Investments Ltd* [1996] AC 415 (PC).

[15] *Madoff Securities International Ltd (in liq) v Raven* [2013] EWHC 3147 (Comm) [188].

[16] *Item Software (UK) Ltd v Fassihi* [2005] 2 BCLC 91 [41].

[17] See eg *Regentcrest plc v Cohen* [2001] 2 BCLC 80 [120]; *Shepherds Investments Ltd v Walters* [2006] EWHC 836 (Ch) [85]. But Matthew Conaglen, *Fiduciary Loyalty: Protecting the Due Performance of Non-Fiduciary Duties* (Hart Publishing 2010) 40-44, 54-58 argues that the directors' best interest duty is not a fiduciary duty because: (1) a trustee's duty to perform the trusts he has undertaken is no different from a legally enforceable duty to act in a particular manner, given that the obligation in both situations is fundamentally contractual in nature; (2) a duty of good faith has been imposed in circumstances that are not traditionally considered fiduciary relationships; and (3) given that the directors' best interest duty is closely analogous to the trustee's duty to perform the trust, it is a not a fiduciary duty. Five rebuttals: (a) his claim that the best interest duty is not a fiduciary duty, while supported by Australian law, is contrary to many English cases (which he recognises in footnote 150 at page 54) and the laws of the common law Asian jurisdiction; (b) a trustee's duty to perform the trust is materially different from a contractual obligation because a trustee, like a director, acts on behalf of the beneficiary and the trustee or director's acts alter the legal position of the beneficiary; in short, a trustee and a director is an agent, but this is not the case for most contractual parties; (c) in the cases he discussed where the party to the contract was

best interest duty is the overarching or foundational fiduciary duty of which the no-conflict rule is a sub-set. This is because compliance with the no-conflict rule increases the likelihood that the best interest duty will be followed.[18] Conversely, a breach of the no-conflict rule is likely to result in a breach of the best interest duty. Thus, it is important to analyse the best interest duty.

Regarding the no-conflict rule, because of the persistent and extensive conflicts of interest between the company on the one hand, and the controlling shareholders in the listed companies in the four common law countries on the other hand, and given the deficient legal mechanisms for regulating the conflicts, it is important to address the question of whether these shareholders should be subject to the no-conflict and no-profit rule.

In addition to the best interest duty and the no-conflict rule, fiduciary duties also comprise the duty to exercise powers for the purposes for which they were conferred. The proper purpose duty is not analysed in this thesis. This is not because controlling shareholders should not be subject to it. Rather, it is because of several reasons. First, the proper purpose duty plays a subordinate and subsidiary role to the best interest duty. A breach of the proper purpose duty is likely to result in a breach of the best interest duty.[19] Second, the proper purpose duty overlaps with the best interest duty. Where neither the company's constitution nor the particular context determines what the proper purpose is, the latter will be determined in

held by the court to be subject to the duty of good faith, the contractual party was not an agent for the other contractual party; (d) the relationship between a trustee and his beneficiary, and a director and the company, has been traditionally considered a fiduciary relationship (*Hospital Products Ltd v United States Surgical Corporation* (1984) 156 CLR 41 [68]) and (e) it does not follow that the duty of good faith has been imposed in situations where there is no fiduciary duty or relationship (i.e. contract cases) that this duty cannot be a fiduciary duty in a specific context, such as that between a director and a company.

[18] Janet Dine and Marios Koutsias, *Company Law* (6th edn, Palgrave MacMillan 2007) 197; Geraint Thomas, *Thomas on Powers* (2nd edn, OUP 2012) 584-5; Lusina Ho, 'Good Faith and Fiduciary Duty in English Law' (2010) 4 *Journal of Equity* 29, 35.

[19] *Permanent Building Society (in liq) v McGee* (1993) 11 ACSR 260. Cf *Hogg v Cramphorn Ltd* [1967] Ch 254, 267-9.

accordance with the interests of the company.[20] Further, the best interest duty and the proper purpose duty are often applied together without distinguishing the two.[21] In light of the first and second reason, and as mentioned above, given that the best interest duty is the core and fundamental fiduciary duty, it would be more profitable to analyse this duty. Finally, a key problem associated with the controlling shareholders in the listed companies in common law systems in Asia lies not in the fact that they have failed to act for proper purposes, but rather in the conflicts of interest between the controllers and the company, which makes it more important to analyse the no-conflict rule.

V. Contributions

First, this thesis challenges a long-standing, fundamental legal principle in English law, and hence the laws in the four common law Asian jurisdictions, that shareholders, unlike directors, should not owe fiduciary duties to the company as they can vote as they please and they are not agents.

Second, although there have been cursory suggestions that fiduciary duties ought to be imposed on controlling shareholders in the common law Asian jurisdictions, this thesis is the first work to develop this idea in a sustained, systematic and comparative way. It does so not only by critically examining why these duties should be imposed, but also, crucially, when controllers should be subject to the duties, who should impose the duties, how the duties can

[20] Rosemary Teele Langford, *Directors' Duties: Principles and Application* (Federation Press 2014) 118-123.

[21] See eg, *Re Smith & Fawcett Ltd* [1942] Ch 304, 306.

be imposed, and how the duties can be enforced. Further, given that the common law Asian systems have generally been neglected in the leading works on comparative corporate law, this thesis fills an important gap as it examines the ownership structures, institutional contexts and shareholders' powers in the four Asian jurisdictions.

Third, this thesis deepens the existing analysis of the legal mechanisms that may be used to address extractions of private benefits of control. It shows that the existing mechanisms which include the use of independent directors and giving decision rights to minority shareholders (such as disinterested shareholder approval) are deficient and defective for the purpose of not only addressing specific transactions in which tunneling is widespread (i.e. related party transactions), but also the broader problem of conflict of interest (which arises not only when controllers exercise formal power through voting but also informal power through the exertion of influence).

Fourth, this thesis advances the debate on a central and fundamental concept in corporate law and governance – the interests of the company – by putting forward the argument that corporate interest need not be equated with shareholders' or stakeholders' interests, but could refer to the long-term value and viability of the company, whose interests are not synonymous with those of shareholders or stakeholders. Drawing on theoretical literature, it is the first comparative work to critically examine this concept by analysing the laws and empirical realities in the four common law jurisdictions in Asia.

Finally, this thesis contributes to the debate on the strategies to promote the long-term success of the company by reconceptualising the role of controlling shareholders as fiduciaries. The current existing and proposed strategies include empowering or incentivising shareholders (such as by giving them greater voting powers, rewarding them with tax benefits or increased dividends)[22] or limiting their rights (such as by suspending voting rights[23] or removing the protection of limited liability under certain circumstances[24]). But none of the strategies critically analyses this question: in whose interests or for whose benefit controlling shareholders ought to exercise the already significant powers conferred on them, in the context of the concentrated ownership structures in common law Asia.

VI. Structure and outline

To make the argument that controlling shareholders in the four common law Asian jurisdictions should be subject to fiduciary duties, I will first explain and critique the current legal position as to why shareholders do not owe fiduciary duties. After that, I will demonstrate why controlling shareholders should be subject to fiduciary duties. Then I will critically analyse the question of what the contents of these fiduciary duties should be. After examining the question of 'why' and 'what', I then analyse the question of 'when' – under what circumstances fiduciary duties should be imposed on controlling shareholders. This is followed by the question of 'who' – by whom the duties should be imposed, i.e. the legislature, courts or the stock exchange. Subsequently, I examine the question of how each of these institutions can

[22] See eg Tamara Belinfanti, 'Shareholder Cultivation and New Governance' (2014) 38 *Delaware Journal of Corporate Law* 789, 845 (suggesting weighted dividends dependent on length or quality of share ownership); Demetra Arsalidou, 'Shareholders and Corporate Scrutiny: The Role of the UK Stewardship Code' (2012) 9 *European Company and Financial Law Review* 342, 376-77 (endorsing France's use of enhanced voting rights).

[23] See eg Lynne Dallas, 'Short-termism, the Financial Crisis and Corporate Governance' (2011) 37 *Journal of Corporation Law* 264; Henry Hu and Bernard Black, 'Equity and Debt Decoupling and Empty Voting II: Importance and Extensions' (2008) 156 *University of Pennsylvania Law Review* 625, 697.

[24] See eg, Paddy W Ireland, 'Limited Liability, Shareholder Rights and the Problem of Corporate Irresponsibility' (2010) 34 *Cambridge Journal of Economics* 837.

impose the duties. Finally, I turn to the question of how breaches of fiduciary duties can be enforced using private and public mechanisms. This thesis comprises seven chapters.

In Chapter 2, I set out the current legal position – shareholders are not subject to fiduciary duties – and I critique the three reasons given for this position: first, votes are property rights and thus shareholders can vote as they please. Second, shareholders can contractually bind themselves to vote as they wish. And finally, the general meeting, unlike the board of directors, is not an agent of the company. I argue that all three reasons are unpersuasive.

In Chapter 3, I first discuss an aspect of corporate governance to which insufficient attention has been paid: the significant legal powers that are wielded by shareholders of the listed companies in the four common law jurisdictions in Asia. I then examine the ownership structure of the listed companies in the four countries and the persistent and serious problem of extractions of private benefits of control by controlling shareholders. Subsequently, I provide three key justifications as to why fiduciary duties should be imposed on controlling shareholders. First, I critically analyse the *ex ante* and *ex post* legal strategies for regulating extractions of private benefits of control by controlling shareholders and I argue that they are all deficient. Second, I argue that the existing law does not regulate other types of conflicts of interest between controlling shareholders and the company that can give rise to extractions of private benefits of control. The third and final justification is that the rationales for subjecting directors to fiduciary duties should also apply to controlling shareholders in the four countries.

In Chapter 4, I examine the contents of the fiduciary duties, i.e. the duty to act in good faith in the best interests of the company, and the duty to avoid unauthorised conflicts and unauthorised receipt of profits (the no-conflict and no-profit rule). Regarding the best interest duty, I develop a theory of the company's interests from a normative, legal and empirical perspective. After examining the notion of the company's interest, I analyse whether the best interest duty should comprise an objective test, subjective test or a combination of both.

Subsequently, I analyse the no-conflict and no-profit rule, and I argue that controlling shareholders should be able to seek authorisation from directors who are neither connected to, nor are the nominees of, the controlling shareholders.

In Chapter 5, I analyse the mechanics of imposing the duties, i.e. when (under what circumstances) controlling shareholders should owe the duties; by whom (the legislature, courts or stock exchange) the duties should be imposed; and finally, how the duties could be imposed by each of these three institutions. I argue that the circumstances that controlling shareholders should be subject to fiduciary duties include the exercise of formal (i.e. corporate) power and informal power (i.e. influence). I then show that different costs and benefits are associated with having different institutions impose the duties. Finally, I argue that the duties could be imposed by the legislature using either a default or mandatory rule; by the courts using the mechanism of shadow/*de facto* directors or on a case-by-case basis; and by the stock exchange through a two-tier regulatory regime.

Chapter 6 analyses how breaches of fiduciary duties by controlling shareholders can be enforced using private and public mechanisms.

Chapter 7 concludes by considering the broader implications of this thesis.

DPHIL CHAPTER 2: WHY SHAREHOLDERS ARE NOT SUBJECT TO FIDUCIARY DUTIES UNDER THE CURRENT LAW

I. Votes are property rights
II. Shareholder can contractually bind themselves to vote as they please
III. Shareholders are not agents of the company
   A. General meeting is a co-agent of the company
   B. General meeting is not a co-agent of the company
   C. Concerns
      1. Agents are not by definition fiduciaries
      2. Problematic to subject all shareholders to fiduciary duties

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It is a well-established legal proposition in the four common law jurisdictions in Asia that unlike directors, shareholders are not subject to fiduciary duties. This proposition is derived from English law. Three reasons have been given in support of this proposition. First, because votes are property rights, shareholders can vote for their own selfish interests even if these are opposed to those of the company. Second, shareholders can enter into legally enforceable contracts to vote in a particular way or not to vote at all. Third, shareholders are not agents of the company. I critically analyse these three reasons and I conclude that they are unpersuasive. Regarding the first reason, I show that no argument has been given as to why votes are property rights. Then I argue that a close analysis of the case law reveals that the real reason why courts held that votes are property rights and thus members can vote as they please is that in most cases, either the interests of the company were not in issue or the outcome did not harm the interests of the company. Regarding the second reason, I argue that it is based on a misinterpretation of the case law. As for the third and last reason, I argue that the view that the general meeting is not an agent of the company is flawed as it is contrary to legal principles and I demonstrate that the view that the general meeting is a co-agent is consistent with the separate legal personality doctrine and agency law. Finally, I addressed concerns with the view that the general meeting is a co-agent.

I. Votes are property rights?

There are numerous obiter remarks in the cases[1], endorsed by commentators[2], that state that a shareholder's right to vote is a property right and thus, he can vote as he pleases, regardless of his motives, and even though his personal interests conflict with those of the company. He can vote in whatever ways he wishes even if doing so is against the company's interests. However, these obiter remarks are nothing but assertions; no argument was given in those cases as to why votes are property rights.

Not all shares (whether ordinary or preferred) necessarily confer voting rights. And if some shares do confer voting rights, those rights are found in the articles of association (and if applicable, subscription contract). These voting rights are contractual rights. Although contract rights can also be property rights, justifications must be given as to why voting rights which are derived from and based on contracts are property rights. But no reason was given by any of the judges who asserted that a shareholder's vote is a property right. The judges merely

[1] *Pender v Lushington* (1877) 6 Ch D 70, 75, 81 (Jessel MR) ('…I have always considered the law to be that those who have the rights of property are entitled to exercise them, whatever their motives may be for such exercise … a man may be actuated in giving his vote by interests entirely adverse to the interests of the company as a whole.') *North-West Transportation Co Ltd v Beatty* (1887) 12 App Cas 589, 593 (PC) (Sir Richard Baggallay) ('every shareholder has a perfect right to vote … although he may have a personal interest in the subject-matter opposed to, or different from, the general or particular interests of the company.') *Burland v Earle* [1902] AC 83, 94 (PC) (Lord Davey).

[2] See eg, Paul L Davies and Sarah Worthington, *Gower Principles of Modern Company Law* (10th edn, Sweet & Maxwell 2016) [19-4], 636-637.

asserted that votes are property rights and then asserted that shareholders can vote as they please.

Importantly, the fact that property consists of a bundle of rights does not mean that the individual rights which constitute that bundle are property rights.[3] The fact that one gets a bundle of rights (including the right to vote) pursuant to owning shares[4] does not entail that those rights are property rights. Indeed, Lord Templeman held that when voting rights have been taken away, the right to vote is not a property right in itself; it is merely an incident of one's ownership of shares.[5]

Further, it is curious that the label of property rights is applied to voting rights but not to other rights such as those governing participation as stated in the articles[6]; the latter have been labelled by courts either as personal rights of members or a matter of internal regularity. Both voting rights and the other types of participatory rights are based on and conferred by the articles. Yet, only voting rights have been characterised as property rights. No explanation has been given (or could sensibly be given) as to why this is the case.

It is submitted that not only are votes not property rights, but a close analysis of the case law reveals that the real reason underlying most of the cases where the courts held that votes are property rights and thus members can vote as they please is this: either the interests

[3] *Belfast Corporation v OD Cars Ltd* [1960] AC 490, 517.

[4] Because, on an influential view, a property right is a right which 'the rest of the world is under a prima facie duty to A not to deliberately or carelessly interfere with a *physical* thing', and given that shares are not physical things, they are not property rights: Simon Douglas and Ben McFarlane, 'Defining Property Rights' in James Penner and Henry Smith (ed), *Philosophical Foundations of Property Law* (OUP 2013) 220, 237-243; William Swadling, 'Property: General Principles' in Andrew Burrows (ed), *English Private Law* (2nd edn, OUP 2007) [4.17]-[4.18]. Shares are not corporeal or physical things because they cannot be equated with the company's assets given the doctrines of separate legal personality and reflective loss; nor are shares interests in the company's assets. See Pretto-Sakmann, *Boundaries of Personal Property: Shares and Sub-Shares* (Hart 2005) 82-93.

[5] *Government of Mauritius v Union Flacq Sugar Estates Co Ltd* [1992] 1 WLR 903, 909H to 910A, 911B to 911H.

[6] The articles stated that if requested by five members, a vote by poll on the adjournment of the general meeting would be required: *Macdougall v Gardiner* (1875) 1 Ch d 13; the articles contained a voting cap that precluded members from voting more than 100 shares regardless of the number of shares owned by the members: *Pender v Lushington* (n 1).

of the company were not in issue (because other interests such as the personal rights of members were at stake) or the outcome did not harm the interests of the company (because the outcome of those cases, where the votes or transactions were challenged, was found to be fair and reasonable). An example of the former can be found in *Pender v Lushington*.[7] Examples of the latter can be found in *North-West Transportation Co Ltd v Beatty*[8] and *Burland v Earle*.[9]

In *Pender v Lushington*, the court found that the failure of the chairman of a general meeting of shareholders to record some of the votes cast by nominee shareholders was a violation of a member's personal right qua members to have his votes counted and recorded. The chairman discriminated against some of the members by denying them the right to have their votes recorded. Jessel MR's obiter assertions that shareholders can vote as they please, regardless of their motives, because votes are property rights,[10] are beside the point. The real issue was whether there was a breach of the personal rights of the shareholders to have their votes recorded as conferred by the articles.

In any event, the bald assertion of property, without any argument, by Jessel MR is question-begging; the assertion did not and could not transform voting rights, which are conferred by the articles and subscription contract, into property rights. And even if votes are property rights, there are not insubstantial restrictions on those rights. It is a trite observation that property rights do not give untrammelled powers to the owner to do anything with his property if the consequence of doing so will harm the interests of others. This was recognised in *Menier v Hooper's Telegraph Works*[11], cited with approval by Jessel MR, where the Court of Appeal held that shareholders cannot vote in such a way as to 'sell the assets of the company

[7] (n 1).

[8] Ibid.

[9] Ibid.

[10] Ibid 75, 81.

[11] (1874) 9 Ch App 350.

and keep the consideration.'[12] Further, shareholders cannot vote to 'appropriate to themselves money, property or advantages which belong to the company, or in which other shareholders are entitled to participate.'[13] Nor are they permitted to vote in transactions that are of a 'fraudulent character or beyond the powers of the company.'[14] And fraud refers not to dishonesty or immorality but '[i]t merely means the power has been exercised for a purpose, or with an intention, beyond the scope of or not justified by the instrument creating the power.'[15] Thus, Jessel MR's stark assertion that members are permitted to vote even if their motives are 'entirely adverse to the interests of the company as a whole'[16], is highly questionable.

In *North-West Transportation,* Beatty who was the director and shareholder sold a steamship to the company. As there was a conflict of interest, the shareholders were required to ratify the sale transaction. In addition to asserting that shareholders can vote as they please (even if doing so were contrary to the company's interests), the court found that: the price was fair, the company needed the steamer, there was no other steamer available, there was no fraud, and the minority was not oppressed. Thus, the interests of the company were not prejudiced by the ratification. The assertion that votes are property rights was besides the point.

In *Burland v Earle*, Burland who was one of the directors and a majority shareholder, made a profit by selling certain property and plant to the company. The claimants sought to disgorge the profits. Apart from affirming *North-West Transportation* and holding that shareholders can vote in transactions in which they are interested[17], the court endorsed (but did

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[12] Ibid 354.

[13] *Burland v Earle* (n 1) 93 (Lord Davey).

[14] Ibid.

[15] *Vatcher v Paull* [1915] AC 372, 378 (Lord Parker).

[16] *Pender v Lushington* (n 1) 75.

not elaborate on) the evidence that (a) the sale price was not unfair to the company[18] and (b) the next largest shareholder 'was present at the sale and knew all about the transaction'[19] (which includes the price that Burland paid for the property and plant). Similar to *North-West Transportation*, there was no evidence that the company's interests were adversely affected by the transaction between the shareholder and the company.

The cases examined above demonstrate that when the court invoked the notion that shareholders can vote as they please, the company's interests were either not prejudiced or not in issue. Had the outcome been harmful to the company's interests, it is submitted that the shareholders' exercise of voting powers would be restricted. Thus, the proposition that shareholders can vote as they please does not provide the critical justification for the result of those cases. It seems to amount to no more than window dressing.[20]

One case, however, that requires explanation is the first instance decision of *Northern Counties Securities Ltd v Jackson & Steeple Ltd*.[21] There, Walton LJ noted that an injunction in another proceeding had been issued against the defendant company ordering it to comply with the contract which it entered into with the claimants to issue shares to the latter and to list the shares on a stock exchange. The defendant company gave an undertaking to the court to issue the shares and obtain a stock exchange quotation. But the defendant failed to comply with the court order and did not discharge its undertaking.

Thus, the claimants applied to the court in the present case to order the defendant company to (a) convene a general meeting to approve the issue of shares, (b) send a circular to

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[17] (n 1) 94.

[18] Ibid 98.

[19] Ibid.

[20] Earl Sneed, 'The Stockholder May Vote as He Pleases: Theory and Fact' (1960) 22 *University of Pittsburgh Law Review* 23.

[21] [1974] 1 WLR 1133.

all members to induce them to vote in favour of the shares and warn them that the failure to do so would amount to a contempt of court, and (c) restrain the directors, in their capacities as shareholders, to vote against the issue of shares.

Walton LJ rejected the contents of the circular. He held that the members, as well as directors voting as members, could vote against the company's contractual obligations and undertaking to the court to issue shares and list them on the stock exchange. Walton LJ said that shareholders in a general meeting are not agents of the company, although their acts bind the company.[22] Also, because they are exercising their own rights of property, they can vote as they please and their acts cannot be regarded as those of the company.[23] Therefore, he is able to arrive at the remarkable conclusion that shareholders in a general meeting can vote as they please and will not be liable for the exercise of their votes, even if they intended to cause the company to violate its undertaking to the court and contractual obligations.[24] He even rejected the claimant's contention that the shareholders' vote would expose the company to proceedings for contempt of court.[25] The effect of his judgment is that the company could circumvent the court order through the acts of general meeting.

Walton LJ's analysis is objectionable on two key levels. First, given that the acts of general meeting will bind the company, it is questionable that shareholders in a general meeting can deliberately cause, direct or authorise the company to violate a court order and breach a contract, and yet not be held liable at all. It is even more questionable that the board of directors can bind the company by entering into a contract; and yet, the shareholders acting in a general meeting is permitted to simply disregard the company's contractual obligations and court order.

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[22] Ibid 1144-1145.

[23] Ibid.

[24] Ibid 1144-1146.

[25] Ibid.

To escape this problem, Walton LJ drew a fallacious distinction between the acts of the shareholders in a general meeting and the acts of the company.[26] He further relied on the notion that shareholders can vote as they please. It is true that shareholders who voted against complying with the court order may not be held personally liable for contempt of court because the liability for contempt rests with the company (as their voting decision is attributed to the company). But one cannot dismiss the possibility (as Walton LJ did) that either the shareholders or directors might be liable for: abetting the company for contempt of court or for inducing the breach of contract, insofar as they have been personally involved in the abetment and inducement to the extent sufficient to attract liability.[27] For example, the directors who were also the shareholders sent out notices to the members in order to induce them to vote against complying with the undertaking and the issue of shares by alleging that the company would save substantial sums of money if the resolutions were not passed. Further, if a company was liable for breaching a contract, its shareholders would be liable for inducing the breach if they had authorised or procured the breach by exercising their powers under the articles.[28] If directors can be personally liable for inducing breach of contract or abetting the company for contempt of court[29], then shareholders who are aware of the contract and court order should not be immune from liability for deliberately preventing the company to discharge those enforceable obligations by voting against the issue and listing of shares.

The second and final objection is this: the failure to curb shareholders' exercise of voting powers could result in them deliberately harming the interests of the company, thereby bringing disrepute to the company and causing it to sustain damages because of the breach of

[26] Walton LJ endorsed the defendant's counsel argument at 1144.

[27] By analogy with directorial liability in *In MCA Records Inc v Charly Records Ltd* [2003] 1 BCLC 93 (CA).

[28] *Southern Foundries (1926) Ltd v Shirlaw* [1940] AC 701, 711.

[29] Brenda Hannigan, *Company Law* (2nd ed, OUP 2009) 69-70.

contract and court order. The extraordinary effect of Walton LJ's reasoning is that the company's contractual obligation and undertaking to the court would be rendered unenforceable by injunction, if shareholders vote against the resolutions to issue the shares and comply with the undertaking, acts which Walton LJ held that shareholders are permitted to do 'whatever its effect may be.'[30] However, if all powers have to be exercised bona fide and for proper purposes[31], then no exception should be made for shareholders' exercise of voting powers unless a compelling justification can be given. Accordingly, the reasoning and result in this case are deeply flawed. This case underscores the problem with the proposition that shareholders can vote as they please.

II. Shareholder can contractually bind themselves to vote as they please

The other argument that ostensibly supports the notion that shareholders can vote as they please is that they are permitted to enter into contracts to vote in certain ways (or not to vote at all) and such contracts are enforceable by injunction. Because shareholders can choose in whose interests they want to vote, or even not to vote at all, they do not owe any fiduciary duties. The case that has been cited to support this proposition is *Puddephatt v Leith*.[32] There,

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[30] *Northern Counties Securities* (n 21) 1144 (Walton LJ endorsed the submissions of the defendant directors' counsel).

[31] *Vatcher v Paull* [1915] AC 372, 378; *Equitable Life Assurance Society v Hyman* [2002] 1 AC 408, 451-62.

[32] [1916] 1 Ch 200 (Ch). This is a first instance decision and one of the shortest ever. The entire case including headnotes and summary has less than 1,200 words.

the claimant borrowed money from the defendant, and under the loan agreement, the claimant mortgaged his shares to the defendant and transferred them to his name. The defendant promised the claimant to vote the shares according to his instructions but he reneged on the promise. The court ordered the defendant to comply with the promise.

This decision was simply a matter of contract law; it is authority only for a simple proposition: undertakings or promises given by one party to another to vote in certain ways (or not to vote at all) are enforceable. But it does not follow from this proposition that shareholders can vote in whichever ways they want to, even if they are antithetical to the company's interests. It may be objected, however, that implicit in the proposition that a shareholder's contractual undertaking to vote in any way required by the promisee includes voting against the company's interests if it is pursuant to the promisee's instructions. But the problem with this argument is that the issue — whether or not a (mandatory) injunction will be granted to compel the shareholder to vote as instructed by the promisee if doing so is opposed to the company's interests — was never raised, let alone decided, in the case. Similarly, although there was nothing in the decision concerning the duties or restrictions that could or should be imposed on shareholders when they exercise their voting powers, it is a logical fallacy to infer from the silence that there are or should be no such duties or restrictions.

There is another first instance decision, however, which might lend support to the notion that shareholders can vote as they please, even if their intent or the effect of which is to harm the company's interests. But it will be argued that this decision is deeply flawed. In *Wilkinson v West Coast Capital*[33], Clause 5 of the shareholders' agreement provides that unless consent from more than 65% of the shareholders is obtained, shareholders have to ensure that the company does not enter into certain transactions. Clause 7 provides that each shareholder

[33] [2007] BCC 717 (Ch).

has to use all reasonable and proper means to promote the company's interests. In order for the directors, who were also the controlling shareholders, to make certain acquisition, the controlling shareholders deliberately blocked the acquisition by not voting to permit the pursuit of those opportunities. Warren J upheld the acts of the controlling shareholders and the acquisition by directors and said that Clause 7 had to be read subject to Clause 5.[34] In a remarkable statement, Warren J said that even if the board of directors held the view that the acquisition was in the company's interests, the directors could still acquire it for themselves because they, acting as shareholders, were entitled to refuse to consent to the acquisition, whose consent was required under the shareholders' agreement.[35] Thus, the minority shareholder failed in his unfair prejudice claim.

Warren J's reasoning leads to problematic consequences. Not only can shareholders vote as they please, but they can also do so in order to deprive the company of valuable opportunities, thereby deliberately harming its interests. Further, directors can be insulated from liability when they acquire certain corporate opportunities, so long as they, acting as shareholders, refuse to consent to the acquisition. The directors will be exempted from liability even if there is a conflict of interest such as where the board has determined that it is in the company's interest to pursue the acquisition. Yet, the directors are permitted to exploit the opportunity. Warren J sought to explain away the conflict by asserting that the shareholders, who are also directors, are under no duty to vote to approve the acquisition, even if it is in the company's interests to do so.[36] The effect of his reasoning is that the company is prejudiced twice. First, the company is not able to undertake the acquisition. Secondly, it cannot sue the directors for breaching their fiduciary duties when they made the acquisition. Admittedly,

[34] Ibid [225].

[35] Ibid [299].

[36] Ibid [299-300].

shareholders can legitimately take a different view on business decisions from directors, and they can express this disagreement though their votes. But there ought to be limits to manifestly self-serving and prejudicial exercise of their votes, particularly on the facts of this case where the interests of the company were clearly harmed. But no such limits appeared to be countenanced by Warren J.

Let us assume that there was no such shareholders' agreement. If the directors, who are also the controlling shareholders, wish to exploit certain opportunities, they may, in their capacity as shareholders, alter the company's articles to include a provision to the effect that consent from certain percentage of shareholders is required for entering into certain transactions. The aim is for the shareholders to withhold consent in order for them as directors to exploit the opportunities. But such alteration to the articles will be subject to the requirement to act bona fide for the benefit of the company as whole.[37]

However, it is highly questionable why such a requirement should not apply to shareholders exercising their voting rights under the shareholders' agreement to decide whether or not to consent to the acquisition, in particular provisions which directly impact on the company's interests, such as Clause 5 in *Wilkinson*. It is no answer to assert that to impose such a requirement will conflict with the proposition that shareholders can vote as they please and they can do so without regard to the adverse effect it would have on the company. This is because if this answer were correct, then shareholders should be able to alter the articles without any restriction. But this is not the case.

Equally important, because shareholders' agreement can amount to a special resolution altering the articles[38], the question is whether there is a principled and coherent justification for confining the requirement to act bona fide in the interests of the company as a whole to the

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[37] *Allen v Gold Reefs of West Africa Ltd* [1900] 1 Ch 656.

[38] *Euro Brokers Holdings Ltd v Monecor (London) Ltd* [2003] 1 BCLC 506.

alteration of articles. This requirement should not depend on the happenstance of whether the provision is in a shareholders' agreement or the altered articles.

In the light of the above analyses, the rule that shareholders can vote as they please, even if their intent or the effect of which is to harm the company's interest, is highly objectionable. Further, the proposition that directors are under a duty to vote in the company's interests, but the very same directors, in their capacity as shareholders, can vote in opposition to the company's interests, thereby undermining or negating the actions of directors and prejudicing the company, is very problematic.

III. Shareholders are not agents of the company

There is another possible reason as to why shareholders do not owe fiduciary duties. In *Bristol & West Building Society v Mothew*, Millet LJ said: 'A fiduciary is someone who has undertaken to act for or on behalf of another in a particular matter in circumstances which give rise to a relationship of trust and confidence.'[39] In a similar vein, Mason J said in *Hospital Products Ltd v United States Surgical Corporation*:

> [t]he accepted fiduciary relationships are sometimes referred to as relationships of trust and confidence or confidential relations… viz., trustee and beneficiary, agent and principal, solicitor and client, employee and employer, director and company, and partners. The critical feature of these relationships is that the fiduciary undertakes or agrees to act for or on behalf of or in the interests of

[39] [1998] Ch 1, 18.

> another person in the exercise of a power or discretion which will affect the interests of that other person in a legal or practical sense. The relationship between the parties is therefore one which gives the fiduciary a special opportunity to exercise the power or discretion to the detriment of that other person who is accordingly vulnerable to abuse by the fiduciary of his position. The expressions "for", "on behalf of" and "in the interests of" signify that the fiduciary acts in a "representative" character in the exercise of his responsibility…[40]

From these two decisions, it is clear that directors are subject to fiduciary duties because they have undertaken or agreed to act on behalf of the company or in the interests of the company. And they have been given discretionary powers which they can exercise to the detriment of the company. But can it be said that shareholders have agreed to act on behalf of the company in the exercise of discretionary power that will affect the legal interests of the company?

To put it succinctly, directors are agents of the company. But can it be said that shareholders acting as general meeting are agents of the company? There are two influential and opposing views concerning whether the general meeting is an agent of the company. The first view states that the general meeting and the board are co-agents of the company, and as agents, they owe fiduciary duties to the company. By contrast, on the second view, the board and the general meeting act as the company and they are not agents of the company, and hence do not owe fiduciary duties. I argue that the first view is more persuasive than the second.

[40] (1984) 156 CLR 41 at [68] (emphasis added). See also *Bristol and West Building Society v Mothew* [1998] Ch 1 at 18 (Millet LJ): 'A fiduciary is someone who has undertaken to act for or on behalf of another in a particular matter…'

A. General meeting is a co-agent of the company

On the first view, the general meeting, like the board of directors, is a co-agent of the company when it makes decisions on behalf of the company to alter its legal position.[41] The authority of the general meeting stems from the statute and the company's constitution.[42] This view is based on three justifications: first, it comports with the legal definition of agency; second, it is a corollary of and gives effect to the fundamental doctrine of separate legal personality; and finally, it is supported by well-established authorities, both from the UK and the common law jurisdictions in Asia.

Agency has been defined as:

> the fiduciary relationship which exists between two persons, one of whom expressly or impliedly manifests assent that the other should act on his behalf so as to affect his relations with third parties, and the other of whom similarly manifests assent so to act or so acts pursuant to the manifestation. The one on whose behalf the act or acts are to be done is called the principal. The one who is to act is called the agent.[43]

A more concise definition is that agency is 'the fiduciary relationship that arises when one person (a "principal") manifests assent to another person (an "agent") that the agent shall

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[41] Peter Watts and FMB Reynolds, *Bowstead and Reynolds on Agency* (20th edn, Sweet & Maxwell 2014) [1-024]. Note that Flannigan argues that shareholders owe fiduciary duties to the company. He asserts that the general meeting could be an agent of the company but his claim that shareholders owe fiduciary duties to the company is not based on agency rather it rests on the basis that authority is granted to the general meeting to make decisions upon incorporation and in light of the company's constitution: Rob Flannigan, "Shareholder Fiduciary Accountability" [2014] *Journal of Business Law* 1, 8.

[42] Watts and Reynolds, ibid.

[43] Ibid [1-001].

act on the principal's behalf and subject to the principal's control, and the agent manifests assent or otherwise consents so to act.'[44]

In sum, it is necessary that one party (i.e. the principal) manifests its assent to have its legal position altered by the other party (i.e. the agent). And secondly, the latter manifests its assent to act or has actually acted.

The agency relationship between the company and the general meeting (or the board) is created through the 'unilateral manifestation by the principal of willingness to have his [or its] legal position changed by the agent.'[45] At the point of the legal incorporation of a company when it becomes a separate and distinct legal entity, the company is legally treated as having assented to the general meeting and the board to make decisions on its behalf, which are legally binding on it. In other words, when the company is legally incorporated, the statute and the company's constitution confer authority on the general meeting to make decisions on behalf of the company, and not as the company. And the company is deemed to have assented to the general meeting doing so (in light of the statute) and has in fact assented (in light of the company's constitution to which the company is a party).

To elaborate, the companies statute and the company's constitution require that certain decisions that alter the legal position of the company could only be taken by the general meeting or the board. For example, the statute only authorises the general meeting (not the board) to approve matters such as those concerning the appointment or dismissal of directors; approval of certain types of transactions between the company and the directors; ratification of breaches of directors' duties; alteration of the company's constitution; appointment of company's auditor; approval of related party transactions; and alteration of the status of a company from public to private. In short, the statute and the company's constitution require or empower the

[44] American Law Institute, Restatement of the Law of Agency, vol. 1 (3rd edn, American Law Institute Publishers 2006) [1.01].

[45] Watts and Reynolds (n 41) [1-006].

general meeting to make certain decisions. And when these decisions are taken by the general meeting, it acts on the company's behalf and alters its legal position as these decisions are legally binding on the company. Likewise for the board, when it makes decisions, it acts on behalf of the company and the decisions alter the company's legal position.

The assent given by the company to the general meeting and the board to alter its rights and obligations has to be imputed to the company. This is because the company, albeit a legal entity that has 'real existence'[46] and is separate and distinct from its members, is an abstraction that is not capable of having any state of mind or knowledge or doing any physical act unless the state of mind or acts of certain persons are ascribed to it.[47]

It is not necessary for the purpose of establishing assent that the company and the general meeting enter into a contract under which the company agrees to be the principal and the general meeting its agent. It suffices if 'the principal manifests to the agent that he is willing for the agent to act, and the agent does so in circumstances indicating that his acts arise from the principal's manifestation'[48], 'even though the first person [i.e. the person conferring the power] cannot be shown to have had, any may indeed not have had, a specific intention of conferring authority.'[49]

The principal's manifestation of assent has to be construed objectively. Thus, at the moment the company is legally incorporated, it is legally treated — in light of the separate personality rule and the powers conferred on the general meeting in the statute and constitution — as having manifested its willingness to have its decisions made on its behalf by the general meeting and accordingly have its legal position altered.

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[46] *Salomon v Salomon & Co Ltd* [1897] AC 22, 33-34.

[47] *Tesco Supermarkets Ltd v Nattrass* [1972] AC 153, 198-199.

[48] Watts and Reynolds (n 41).

[49] Ibid [1-007].

It is necessary but insufficient, however, that the company manifests assent to the general meeting to act on its behalf. The general meeting must also either manifest assent to act or has acted under the manifestation. The general meeting is legally treated as having manifested its assent to act because the statute and the constitution requires or empowers it to make certain decisions that affect the company's rights and obligations. Alternatively, the general meeting has acted pursuant to the manifestation when it in fact takes a decision that alters the legal position of the company. In either of these two situations, the general meeting is the company's agent.[50]

The crucial connection between the separate legal personality rule and the general meeting as an agent who acts on behalf of the company and alters its legal position can be further explained in this way. As an illustration, consider one of the corollaries of the separate legal personality rule: the assets of the company are owned by the company, not by shareholders who merely own shares. Prior to the 1840s, joint stock companies were considered large partnerships and partnership law generally applied to them.[51] This meant that members of the joint stock company were effectively principals and agents of each other, i.e. they owed fiduciary duties to each other. Moreover, shares were considered equitable interests in the company's assets. This meant that shareholders had an interest in the company's assets.

However, in light of the economic and legal changes that culminated in the recognition of the company as a real legal entity that is distinct and separate from its members in *Salomon v A Salomon & Co Ltd* [1897] AC 22[52], shareholders were no longer treated as principals and agents of each other (and hence no longer owed each other fiduciary duties) and they were no

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[50] Ibid [2-033].

[51] Paddy Ireland, 'Finance and the Origins of Modern Company Law' in Grietje Baars and Andre Spicer, *The Corporation* (CUP 2017) 239-240.

[52] Ibid 240-243.

longer regarded as equitable owners of the company's assets. Instead, it is the company who owns the assets and to whom duties are owed. This has critical consequence for how the assets of the company ought to be dealt with by the board or the general meeting. When the board of directors makes a decision concerning the management of the company's assets, it is acting on behalf of the company, for the purpose and benefit of the company. The same logic applies if it is the general meeting which is tasked with managing the company's assets. For example, the listing rules in the UK[53] and common law jurisdictions in Asia[54] require significant or major transactions, the value of which exceed certain percentage of the company's assets, to be approved by the general meeting. Hence, when the general meeting decides whether or not to approve a significant transaction, say a disposal of the company's assets, it is not acting as the company. Nor is the general meeting acting on behalf of shareholders. Rather, it is acting on behalf, and for the benefit, of the company. This is because these assets belong to the company – a real, separate and distinct legal personality – and not to the shareholders. Likewise, when the general meeting decides whether to approve either a proposed loan from a company to the directors or a proposed guarantee by the company for the directors, the general meeting is acting on behalf of the company and has to do so for the latter's benefit. This is a consequence of the fundamental rule of separate legal personality.

Another important consequence of the separate legal personality rule is that duties are owed to the company, the result of which is that only the company can ratify breaches of, or enforce, the duties that are owed to it. Accordingly, because the company is a legal abstraction and a separate legal entity, it can only act through its agents, and thus, when the company through its general meeting ratifies breaches of directors' duties, the general meeting is acting

[53] UKLA Listing Rules, 10.2.2, 10.5.1

[54] HKEX LR 14.06(3), 14.40, 14.44, 14.46; SGX LR 1014(2), LR 1015(1)(b); Bursa Malaysia LR 10.07; India Companies Act 2013 (IN CA), s 180.

on behalf of the company; it is not acting 'as' the company, let alone on behalf of shareholders. Moreover, if it were true that the general meeting is acting as, and not on behalf of, the company, it should be able to ratify all kinds of breaches of duties by directors. But this is not true as the general meeting can commit a fraud on the company if it were to ratify certain breaches.[55] The fraud on the company (or imprecisely put, fraud on the minority[56]) doctrine suggests that the general meeting owes duties to the company to ensure that the ratification is carried out for proper purposes (so that the company is not (unjustifiably) harmed). This suggests that the general meeting is acting on behalf, rather than as, the company. Similarly, because shareholders are acting on behalf of the company when they pursue a statutory derivative action, the court has to decide whether it appears prima facie in the company's interests for leave to be granted.[57]

To look at it from a different angle, if the assertion that the general meeting acts as the company (rather than on its behalf) is correct, the general meeting should have the ability to approve the exclusive use or appropriation of the company's assets for its own benefit, as and when it wishes to. But if the general meeting were to approve (even if on a unanimous basis) the distribution of the company's assets among the shareholders, this could amount to criminal misappropriation of property and a violation of the capital maintenance rule.

One possible objection is that because the shareholders benefit from the general meeting's decision as to, for example, whether to permit the company to dispose of its property or to engage in transactions with directors, or whether to ratify breaches of directors' duties, it

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[55] Len Sealy and Sarah Worthington, *Sealy and Worthington's Cases and Materials in Company Law* (10th edn, OUP 2013) 640.

[56] *Burland v Earle* [1902] AC 83, 93; *Atwool v Merryweather* (1867) LR 5 Eq 464n; *Menier v Hooper's Telegraph Works* (1874) 9 Ch App 350; *Cook v Deeks* [1916] 1 AC 554.

[57] Singapore Companies Act (Cap 50) (SG CA), s 216A(3)(c); Malaysia Companies Act 2016 (MY CA), s 348(4)(b); Hong Kong Companies Ordinance (Cap 622) (HK CO), s 733(1)(a).

cannot be said that the general meeting is an agent because the benefit accrues to the shareholders and not to the principal (i.e. the company). Thus, the general meeting is not an agent as it does not act on behalf and for the benefit of the company. This objection is misguided. The shareholders themselves or the individual shareholder himself may benefit from those decisions, but only derivatively; 'shareholder gain is reflected gain'.[58] Shareholders' gains (or losses) from the general meeting's decisions are derived from corporate gains (or losses).[59] Reflective gain (or loss) is a corollary of the separate legal personality rule.

At this juncture, it is apt to clarify why an individual shareholder (as opposed to the general meeting) is not an agent of the company. This is because a shareholder alone (unless it is a one-man company) is incapable of acting on the company's behalf and altering its legal position; its decision alone is incapable of binding the company. Rather, it is the general meeting who is an agent of the company because it is acting on the company's behalf, and makes decisions that alter the legal position of, and bind, the company. But not all decisions taken by shareholders bind the company and alter the company's legal position. For example, when shareholders alter the rights related to a class of shares, a matter concerning intra-shareholders, they are not acting on the company's behalf. Another example is when shareholders exercise their rights to inspect the company's documents.

However, it may be queried why the board of directors, as well as an individual director, is an agent of the company, whereas only the general meeting is an agent of the company, but not an individual shareholder or group of shareholders. The answer is this: an individual director is an agent of the company because the law permits the board to delegate its authority to that director to act on the company's behalf. The same logic applies to a committee of

[58] Flannigan (n 41) 10.

[59] Shareholders cannot claim for reflective loss unless it amounts to personal losses: *Johnson v Gore Wood & Co* [2002] 2 AC 1.

directors (such as the audit or nominating committee) who is also an agent of the company as it has been delegated authority by the board to act on the company's behalf. But in the case of an individual shareholder or a group of shareholders, it has not been delegated authority by the general meeting to act on the company's behalf.

Finally, to reject the view that the general meeting is an agent who acts on behalf of the company and to instead adopt the view that the general meeting acts as the company implies that the general meeting or the board either embodies or is the company (i.e. it is an organ of the company). However, this contradicts the separate legal personality doctrine. If the general meeting were indeed acting as the company, it should be able to appropriate the company's assets for itself, without regard for the company's interests; this is however contrary to the law. It is well-established that a sole shareholder or the whole body of shareholders cannot 'validly consent to their own appropriation of the company's assets for purposes which are not the company's'.[60]

Last but not the least, the principle that the company is the principal and can only act through its agents has been repeatedly affirmed in numerous English decisions that stretched all the way back to the nineteenth century[61] and persisted to modern times.[62] This view has

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[60] *Prest v Petrodel Resources Ltd* [2013] 2 AC 415 [41].

[61] *Yarborough v The Bank of England* (1812) 16 East 6 (KB) 7, 104 ER 991 (Lord Ellenborough CJ) ('As a corporation, they can do no act, not even affix their corporate seal to a deed, but through the instrumentality and agency of others'); *Aberdeen Railway Company v Blaikie Brothers* (1854) 1 Macq 461, 471 (Lord Cranworth LC) ('The directors are a body to whom is delegated the duty of managing the general affairs of the company. A corporate body can act only by agents'); *Ferguson v Wilson* (1866) LR 2 Ch App 77, 89 (Cairns LJ) ('What is the position of directors of a public company? They are merely agents of a company. The company itself cannot act in its own person, for it has no person; it can only act through directors, and the case is, as regards those directors, merely the ordinary case of principal and agent'); *Citizen's Life Assurance Company Limited v Brown* [1904] AC 423, 426 (Lord Lindley) ('If it is once granted that corporations are for civil purposes to be regarded as persons, ie as principals acting by agents and servants, it is difficult to see why the ordinary doctrines of agency and of master and servant are not to be applied to corporations as well as to ordinary individuals').

[62] *Freeman & Lockyer v Buckhurst Park Properties Ltd* [1964] 2 QB 480, 504 (Diplock LJ) ('a corporation cannot do any act, and that includes making a representation, except through its agent'); *Tesco Supermarkets Ltd v Nattrass* [1972] AC 153, 198-199 (Lord Diplock) ('A corporation is an abstraction. It is incapable itself of doing any physical act or being in any state of mind. Yet in law it is a person capable of exercising legal rights and of being subject to legal liabilities which may involve ascribing to it not only physical acts which are in reality done

even been endorsed recently in the UK Supreme Court.[63] Importantly, there are cases in the common law jurisdictions in Asia that lend support to this view.[64]

B. General meeting is not a co-agent of the company

By contrast, the second view rejects the argument that the general meeting and the board are co-agents of the company. On this view, the general meeting and the board act *as* the company[65] for they are organs.[66] This view is based on two reasons, the first of which is that directors were no longer the company's agent in light of the recognition of the constitutional division of powers between the board and the general meeting, and the second is the primary

by a natural person on its behalf but also the mental state in which that person did them. In civil law, apart from certain statutory duties, this presents no conceptual difficulties. Under the law of agency the physical acts and state of mind of the agent are in law ascribed to the principal, and if the agent is a natural person it matters not whether the principal is also a natural person or a mere legal abstraction') (cf Lord Reid at 169 who endorsed the organ theory); *Petrodel Resources Ltd v Prest* [2012] EWCA Civ 1395 [18] (Rimer LJ) ('Those who control [a company's] affairs— even if the control is in a single individual— act merely as the company's agents') affirmed [2013] UKSC 34, [2013] 2 AC 41.

[63] *Jetivia SA v Bilta (UK) Ltd* [2016] AC 1 [183] (Lords Toulson and Hodge) ('Because the company is not a natural person it can operate only by the acts of its officers, employees and agents' (Lords Toulson and Hodge cited with approval *Aberdeen Railway Company v Blaikie Brothers* (1854) 1 Macq 461, 471; *Ferguson v Wilson* (1866) LR 2 Ch App 77, 89; *Citizen's Life Assurance Company Limited v Brown* [1904] AC 423, 426.

[64] See eg, *Peringkat Istimewa Sdn. Bhd. v Pua Kim An* [2016] AMEJ 2279 [36] ('The directors are a body to whom is delegated the duty of managing the general affairs of the company. A corporate body can only act by agents, and it is, of course, the duty of those agents so to act as best to promote the interests of the corporation whose affairs they are conducting'); *Rangachari v Bharat Sanchar Nigam Limited* 2007 Indlaw SC 1076 [17] ('A company can only act by agents, and usually the persons by whom it acts and by whom the business of the company is carried on or superintended are termed directors…. Directors are, in the eye of the law, agents of the company for which they act, and the general principles of the law of principal and agent regulate in most respects the relationship of the company and its directors'); *Tai Kam San & Anor v Lim Cher Kia* (2001) MSCLC 97402, [28] ('The law generally treats a company director, being its trustee and agent as a fiduciary').

[65] Davies and Worthington (n 2) [7-4].

[66] Sarah Worthington, *Sealy & Worthington's Text, Cases & Materials in Company Law* (11th edn, OUP 2016), 188.

rules of attribution articulated in the Privy Council decision in *Meridian Global Funds Management Ltd v Securities Commission* (*Meridian*).[67]

It has been argued that the view that the board is an agent of the company 'seems not to have survived the early twentieth century re-characterisation of the articles as a constitution, dividing the powers between the shareholders collectively and the board.'[68] The reasoning is this.[69] Prior to the twentieth century, the board was considered an agent of the company who was ultimately subject to the power of the general meeting, the latter of whom could dictate to the board how they could exercise their powers.[70] However, subsequently, courts held that where the company's constitution, properly construed, has conferred powers upon the board of directors, the general meeting could not interfere with the exercise of powers by the board (except by altering the company's constitution or dismissing the directors).[71] Therefore, the board is not an agent of the company subject to the latter's control through the general meeting. Accordingly, since the board is not an agent of the company, so is the case of the general meeting.

However, whether the board or the general meeting is an agent of the company is a conceptually separate issue from whether the general meeting can interfere with the exercise of powers by the board. Nothing in the nineteenth century authorities or subsequent case law that held that the company can only act by agents raised, let alone examined, the issue of whether shareholders can interfere with the powers of management conferred on directors in the articles. Further, the cases that have affirmed the principle that neither the board nor the

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[67] [1995] 2 AC 500.

[68] Davies and Worthington (n 2) footnote 4, p. 152.

[69] Ibid [14-5]-[14-6].

[70] *Isle of Wight Railway v Tahourdin* (1883) 25 ChD 320, 329.

[71] *Automatic Self-Cleansing Filter Syndicate Co v Cuninghame* [1906] 2 Ch 34; *Shaw & Sons (Salford) Ltd v Shaw* [1935] 2 KB 113.

general meeting can encroach upon each other's constitutionally allocated powers make no mention of whether the board or the general meeting is an agent of the company.

However, it might be rebutted that if the board is an agent of the company, the implication is that the latter has control over the former. And who is the company in this instance but the shareholders themselves? It follows that the company acting through the shareholders have control over the exercise of powers by the directors, which entail that they can interfere with the directors' decisions. But because the general meeting could no longer do that, directors are no longer agents of the company.

The response to the rebuttal is this: it is true that under agency law, a principal has control over the agent in the sense that it can increase, decrease, or modify the scope of authority that it has conferred on the agent. In the context of company law, in order for the company to change the scope of the board's authority, the proper way to do it is for the company to alter the constitution[72]; the general meeting cannot change the scope of directorial authority by simply overriding or disregarding the board's decisions. After all, the authority of the board is derived in part from the company's constitution, which is an agreement entered into between the company and its shareholders. And in order for the company to alter its constitution, it has to do so through the general meeting because first, the companies statute only permits the general meeting to alter the constitution[73], and secondly, the company as a legal abstraction can only act through an entity which is the general meeting in this particular instance, who will decide on behalf of the company and whose decision will alter its legal position. Thus, it is consistent to subscribe to these two views concurrently: (a) the company has control over the authority of its agent, i.e. the board of directors, and (b) and the control is

[72] *Shaw & Sons (Salford) Ltd v Shaw* [1935] 2 KB 113.

[73] UK Companies Act 2006, s 21; HK CO, s 88; SG CA, s 26; IN CA, ss 13, 14; MY CA, s 36.

carried out through the general meeting, which acts on the company's behalf to alter the constitution and is therefore its agent.

The second reason for the view that neither the board nor the general meeting is an agent of the company is that Lord Hoffmann distinguished between the primary rules of attribution (i.e. the decisions of the board and the general meeting) and the general rules of attribution (i.e. the rules of agency and vicarious liability). It has been asserted that the basis for the view that the board and general meeting are organs and act as but not on behalf of the company is Lord Hoffmann's rules of attribution.[74] Further, it might be said that if the board or the general meeting is an agent of the company, then it would seem that the primary rules of attribution are redundant. Lord Hoffmann could have simply reduced the rules of attribution to two categories, the general rules and special rules of attribution. The fact that he distinguished three categories of rules of attribution (i.e. primary, general and special) suggests that the first category consisting of the primary rules is distinct from and should not be reduced to the second consisting of the general rules.

However, Lord Hoffmann never said that the board or the general meeting is not an agent of the company.[75] Furthermore, his primary rules of attribution are consistent with agency law as these rules merely restate the well-established agency principle that the company can confer actual authority on the board via the constitution.[76]

Equally if not more important, there are four difficulties with the view that the general meeting is an organ and with the reliance on *Meridian*. First, Lord Hoffmann implied in

[74] Worthington (n 66) 188.

[75] Watts and Reynolds (n 41) [1-024].

[76] *Freeman & Lockyer v Buckhurst Park Properties Ltd* [1964] 2 QB 480, 504; Peter Watts, 'Directors as Agents: Some Aspects of Disputed Territories' in Danny Busch and others, *Agency Law in Commercial Practice* (OUP 2016) 101.

Meridian[77] that the decisions of the board or the general meeting constitute decisions *on behalf of the company*. This implication is clear from his statement that '[n]ot every act on behalf of the company could be expected to be the subject of a resolution of the board or a unanimous decision of the shareholders.'[78] If the board and general meeting are organs of the company, then its decisions could not be made on the company's behalf, which is contrary to Lord Hoffmann's dictum. Further, it has been remarked that the board as an organ of the company is the basis of the primary rule of attribution expounded by Lord Hoffmann in *Meridian*.[79] If this is correct, it follows that an organ acts as, but not on behalf of, the company. But Lord Hoffmann said precisely the opposite.

Second, judges who have endorsed the idea that the board (or the general meeting) is an organ of the company have derived support for their position in part from German law,[80] which is inconsistent with English common law. Lord Walker[81] said that the precursor of *Meridian* is *El Ajou v Dollar Land Holdings Ltd*[82] where Lord Hoffmann, in discussing *Lennard's Carrying Co. Ltd v Asiatic Petroleum Co. Ltd*[83], observed that under German law, the agents and organs of the company are distinguished, with the directors regarded as the company's organs and as representing the company.[84] Lord Walker interpreted Lord Hoffmann's statements in *El Ajou* as meaning that '[English law] does regard a company's

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[77] *Meridian* (n 67).

[78] Ibid 506.

[79] *Moulin Global Eyecare Trading Ltd v Commissioner of Inland Revenue* [2014] HKEC 419 [64] (Lord Walker).

[80] Susan Watson, 'Conceptual Confusion: Organs, Agents and Identity in the English Courts' (2011) 23 *Singapore Academy of Law Journal* 762 [32].

[81] *Moulin Global Eyecare Trading Ltd v Commissioner of Inland Revenue* [2014] 3 HKC 32 HKCFA [64].

[82] [1994] 2 All ER 685.

[83] [1915] AC 705.

[84] Ibid 705.

board of directors, as a body, as the company's vital organ. That is the basis of the primary rule of attribution which he expounded, soon afterwards, in *Meridian*.'[85] But those who seek to derive support for their view that the board (or general meeting) is an organ but not an agent from the primary rules of attribution should note that neither Lord Hoffmann in *Meridian* nor Lord Walker explained how the view that the board is an organ of the company is consistent with the well-established authorities[86] that stated that the company can only act through agents, of which the board of directors is one. In other words, if Lord Hoffmann or Lord Walker had intended to repudiate the authorities that affirm the view that the company can only act through agents, they would have said so. But nothing in their judgments evinced such an intention.[87]

Third, the concept of organ is either doubtful in its analytic value or incoherent. Lord Hoffmann asserted that under English law, 'whether a person is an organ or not depends upon the extent of the powers which in law he has express or implied authority to exercise on behalf of the company.'[88] This implies that a general meeting, like the board, is an organ of the company because it has been conferred authority to exercise significant powers on the company's behalf. In short, in order to be an organ, it must first be an agent.[89] If that is the case, what is the distinctive analytic value of having the concept of organ? If it is merely used to underscore the importance of certain kinds of agents in company law (i.e. the board and the general meeting), it is unnecessary to introduce the concept of organ. Unsurprisingly, the

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[85] (n 81).

[86] (n 61)-(n 63).

[87] Watts (n 76) 101.

[88] *El Ajou* (n 82) 705.

[89] *Northside Developments Pty Ltd v Registrar-General* (1990) 170 CLR 14 [64] (Dawson J) ('But the organic theory merely extends the scope of an agent's capacity to bind a company and there must first be authority, actual or apparent. It is only then that a person may be regarded not only as the agent of a company, but also as the company itself — an organic part of it — so that "[t]he state of mind of [the agent] is the state of mind of the company": *H.L. Bolton (Engineering) Co. Ltd. v. T.J. Graham & Sons Ltd.* [81], per Denning L.J. Thus the application of the theory depends in the first instance upon there being authority, that is to say, agency….').

concept of organ does not have doctrinal status under English company law or the laws of the four common law countries in Asia, unlike agency. More importantly, it is incoherent to claim that on the one hand, the concept of organ depends on agency law, and on the other hand, the concept of organ necessarily precludes the application of agency law. This is because under German law (on which the view that the board and general meeting is an organ is based), the board and the general meeting ('Aktiengesellschaft') are treated as 'integrated parts of the corporation organism itself'[90] and thus, the acts of these organs are '… *automatically* the act of the juristic person [i.e. the company]'[91], which '… leads *necessarily* to the exclusion of the rules of agency as far as "organ-acts" are concerned.'[92]

Finally, at a fundamental level, the doctrine of separate legal personality and the rules of attribution call into question the assertion that the general meeting is an organ of the company and acts as the company. To claim that the general meeting is an organ of the company implies that it is an intrinsic and internal part of the company. This is inconsistent with the doctrine of separate legal personality which clearly establishes that the company is distinct and separate from its shareholders and directors. To assert that the general meeting, as an organ, acts *as* the company (as opposed to on its behalf), is not an accurate way of expressing the legal principle that the acts of the general meeting (or the acts of the board of directors) are attributed or attributable to the company (under certain circumstances and for certain purposes). To say that the decisions of a majority vote of shareholders, or decisions of the board, 'shall be' or 'are' decisions of the company, is merely an abbreviated and imprecise way of expressing the legal principle that the decisions of the general meeting (or the board) are

[90] Dieter Eckert, 'Shareholder and Management: A Comparative View on Some Corporate Problems in the United States and Germany' (1960) 46 *Iowa Law Review* 12, n 5.

[91] Ibid (emphasis added).

[92] Ibid 18 (emphasis added).

attributed to the company under certain circumstances. In other words, if the general meeting (or the board) is indeed an organ of the company who acts *as* the company, or if the acts of the general meeting (or the board) indeed *are* those of the company, then the rules of attribution would be redundant. The rules of attribution fundamentally presuppose that the general meeting is distinct and separate from the company (i.e. it is not an organ of the company) and therefore, rules are required to attribute the acts of the former to the latter.

Before concluding the analysis on why the second view is problematic, it should be acknowledged that dicta could be found in the cases in the common law countries in Asia that have endorsed the view that the board and the general meeting are organs and they therefore act as the company.[93] Unsurprisingly, the courts in these countries have based this view on English case law where the English judges in turn derived the organic view from German law.[94] The reasoning of these English cases has been criticised and to the extent that courts in the common law countries in Asia relied on it, it is highly questionable.

Accordingly, for the reasons given above, the view that the general meeting is an agent of the company when it acts on the company's behalf and alters its legal position is more persuasive than the view that the general meeting is an organ of, and hence acts as, the company.

Descriptively, the view that the general meeting is a co-agent of the company is able to explain why, as matter of law, shareholders are given voting powers. To be clear, because the general meeting is an agent, shareholders are given voting powers. The reverse is incorrect, namely, given that shareholders are given voting powers, the general meeting is an agent. This is because an agent acts on the principal's behalf and alters the latter's legal position by making legally binding decision. In order for shareholders to make such decisions, they have to act in

[93] See eg, *Gabriel Peter & Partners v Wee Chong Jin* (1998) MSCLC 96719 [25]; *Amer Singh Bhatt v Kelana Resorts Sdn Bhd* [2007] AMEJ 0005, 10-11; *Cyrus Investment Private Limited and another v Tata Sons Limited and others* 2017 Indlaw NCLAT 19 [95].

[94] *Lennard's Carrying Co. Ltd v. Asiatic Petroleum Co. Ltd* [1915] AC 705, 713–714.

a general meeting by voting on matters that they have been authorised to do so under the statute and company's constitution. Therefore, shareholders are given voting rights. The general meeting is an agent not because it has voting powers: after all, shareholders do not always act on the company's behalf and alter its legal position when they vote, an example of which is when shareholders of a class vote to alter their rights attached to the class of shares which they are owners.[95] In sum, the view that shareholders are given voting powers because the general meeting is an agent is based on and comports with legal doctrines – the separate legal personality rule and agency law.

C. Concerns

There are however at least two concerns that may cast doubt on the above analysis. First, because an agent is not a fiduciary in certain situations, the claim that agents are by definition fiduciaries is called into question. The second concern is that to accept the claim that the general meeting owes fiduciary duties would require all the shareholders who voted in the meeting to be subject to fiduciary duties but this is impracticable and problematic.

1. Agents are not by definition fiduciaries

[95] Although shareholders are not agents of the company, and hence do not owe fiduciary duties, when they vary their own class rights, it does not follow that no restriction is imposed on these shareholders. Dissatisfied shareholders may apply to the court to cancel the alteration and the court may do so if it is satisfied that it causes unfair prejudice to the affected shareholders: SG CA, s 74(1) and (4); HK CO, s 182; IN CA, s 48(2); MY CA, s 93(1).

In response to the first concern, because an agent can alter the principal's legal position and can materially and adversely affect the latter's rights and obligations, it is appropriate to subject agents to fiduciary duties.[96] Indeed, '[t]he critical feature of [fiduciary] relationships is that the fiduciary undertakes or agrees to act for or on behalf of or in the interests of another person in the exercise of a power or discretion which will affect the interests of that other person in a legal or practical sense.'[97]

Moreover, the general rule that an agent owes fiduciary duties to the principal could be qualified to take into account the fact that because the scope of duties may vary in different circumstances, an agent in a particular circumstance may not owe fiduciary duties to the principal.[98]

Further, even if we do not adopt the approach of articulating and endorsing a definition of an agent and instead adopt the approach of identifying the circumstances or features that give rise to fiduciary relationships[99], the general meeting still owes fiduciary duties to the company under the latter approach. Consider three general characteristics of relationships where fiduciary duties have been imposed: (1) the fiduciary is able to exercise some power; (2) the fiduciary can unilaterally exercise that power to affect the beneficiary's legal or practical interests; and (3) the beneficiary is vulnerable to the fiduciary who wields the power.[100]

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[96] Watts and Reynolds (n 41) [6-037].

[97] *Hospital Products Ltd v United States Surgical Corporation* (1984) 156 CLR 41 [68] (Mason J). See also *Bristol and West Building Society v Mothew* [1998] Ch 1 at 18 (Millet LJ) ('A fiduciary is someone who has undertaken to act for or on behalf of another in a particular matter…').

[98] Watts and Reynolds (n 41) [6-037].

[99] *Phipps v Boardman* [1967] 2 AC 46, 127 (Lord Upjohn); *Re Coomber* [1911] 1 Ch 723, 728-729 (Fletcher Moulton LJ).

[100] *Frame v Smith* [1987] 2 SCR 99, 136. Note that the element of vulnerability to abuse mentioned by Mason J and Bertha Wilson J is 'not the hallmark of fiduciary relationship' although it is an indicator: *Hodgkinson v Simms* [1994] 3 SCR 377, 405.

Applying these three characteristics to the context of the general meeting, it undertakes (or is treated under the law by virtue of incorporation and the statute as having undertaken) to act on the company's behalf; shareholders can exercise discretionary powers as they can choose whether or not to attend the general meeting and whether or not to vote; the general meeting can unilaterally exercise that power or influence, thereby affecting the principal's interests; and the company is vulnerable to the shareholders acting in general meeting who wield the discretionary power or influence.[101] One glaring example of vulnerability was provided for in the 2012 Kay Review that was tasked by the government to review the UK equity markets and its impact on the long-term performance and governance of UK listed companies. The Kay Review concluded that short-termism is a problem. Among the examples given, the Kay Review noted that the general meeting of GEC, Britain's top electrical company in the late 1960s, approved a series of disposals and acquisitions in order to maximise share price, the result of which was that the company subsequently became insolvent and was wound up.[102] In a remarkable indictment, the Kay Review stated that '[m]any of the bad decisions described [in the Review] were supported or even encouraged by a majority of the company's shareholders.'[103]

[101] Vulnerability occurs not only when the general meeting makes decisions that are contrary to the company's interests, but also when shareholders exercise informal influence such as by threatening to dismiss directors who refuse to do their bidding. The Company Law Review Steering Group noted that managers were pressurised by shareholders to pursue short-term gains: Company Law Review, *Modern Company Law for a Competitive Economy*: The Strategic Framework (DTI, 1999) para 5.1.10. The National Association of Pension Funds reported that institutional investors instructed boards to pursue short-term gains: see National Association of Pension Funds Limited, *Institutional Investment in the UK: Six Years On* (November 2007) 25.

[102] John Kay, *The Kay Review of UK Equity Markets and Long-term Decision-Making, Final Report* (London: Department of Business, Innovation and Skills, 2012) ('Kay Review') para 1.16.

[103] Ibid para 1.28.

2. Problematic to subject all shareholders to fiduciary duties

The second concern – it is impracticable to subject all the shareholders who voted in the general meeting to fiduciary duties – rests on a misconception of how shareholders make valid and binding decisions on behalf of the company. A shareholder (unless he or she is a one-man company) cannot act on the company's behalf. The authority to exercise corporate power on behalf of the company is conferred by the statute and the company's constitution on a duly convened general meeting comprising shareholders who are eligible to vote. Authority is not conferred on an individual shareholder or certain shareholders. An individual shareholder or certain shareholders do not have authority to make valid and binding decisions on the company's behalf unless it is expressly provided for in the statute and constitution. Even if a shareholder owns more than 50% of the shares, and the decision to be taken only requires ordinary resolution, that shareholder does not and cannot unilaterally make a valid and binding decision on the company's behalf except through a duly convened general meeting which will comprise other shareholders. To say that the general meeting is subject to fiduciary duties does not entail that every single shareholder who voted at the meeting is subject to fiduciary duties. A single shareholder would be subject to fiduciary duties only if he or she has the power to alter the legal position of the company, i.e. power has been conferred on a single shareholder to make valid and binding corporate decision. But under the law, power is not conferred on a single shareholder to make corporate decision. It is conferred on the general meeting. The implication of conferring power on the general meeting to make decision on the company's behalf is that only the general meeting, not the individual shareholders who voted at the meeting, will be subject to fiduciary duties.

Two consequences thus arise. First, a shareholder who acted against the company's interests by voting (for or against) a particular resolution will not be in breach of fiduciary duties on the basis that the general meeting is an agent of the company. If we want to hold individual shareholders or a particular type of shareholder liable, we need a different basis; breach of duties arising from agency does not provide the justification. This is why in Chapters 3, I advance legal and policy justifications, not based on agency, to support my argument that fiduciary duties should be imposed on controlling shareholders. The second consequence is that a minority or dissenting shareholder who alleges that the general meeting has breached its fiduciary duties cannot sue individual shareholders for breach of fiduciary duties that arise out of the general meeting being an agent. What the minority shareholder could do is to sue the general meeting for breach of fiduciary duties and ask the court to invalidate the resolution that has been approved at the general meeting[104], or if the resolution has yet to be approved, to seek an injunction. However, if the minority shareholder would like to sue a particular shareholder such as the controlling shareholder, the basis does not lie on the notion that the general meeting has breached its duties as an agent. Rather, it rests on the notion that controlling shareholders should be subject to fiduciary duties, which requires justifications that are not concerned with agency (see Chapter 3). The mechanisms for enforcing such a claim will be examined in Chapter 6.

To conclude, this section demonstrates that a key reason in support of the proposition that shareholders do not owe fiduciary duties to the company, i.e. the general meeting is not an agent of the company (unlike the board of directors), is unpersuasive. But it does not follow that the general meeting is an agent of the company and hence owes fiduciary duties to the company that an individual shareholder, such as a controlling shareholder, is also a fiduciary.

[104] Minority shareholders have successfully sought to invalidate resolutions that had been passed (albeit in a different context): *Clemens v Clemens Bros Ltd* [1976] 2 All ER 268 (Ch); *Dafen Tinplate Co Ltd v Llanelly Steel Co* (1907) Ltd [1920] 2 Ch 124.

Different and separate legal and policy justifications have to be given in order to justify the claim that controlling shareholders should owe fiduciary duties to the company. In the next chapter, I will provide these justifications. The purpose of this chapter is merely to show that the reasons given in support of the view that shareholders do not fiduciary duties are unpersuasive. Although demonstrating that these reasons are unpersuasive does not in itself establish that controlling shareholders should owe fiduciary duties, this analysis is important because any argument that seeks to impose fiduciary duties on shareholders or a specific group of shareholders has to first explain why the current legal position, namely, shareholders are not subject to fiduciary duties, is unpersuasive. It is a basic legal hurdle that has to be cleared first.

DPHIL CHAPTER 3: WHY CONTROLLING SHAREHOLDERS SHOULD BE SUBJECT TO FIDUCIARY DUTIES

I. Shareholders wield significant legal powers

II. Concentrated ownership and extractions of private benefits of control
  - A. Hong Kong
    1. Family-owned companies
    2. State-owned enterprises
  - B. Malaysia
    1. Family-owned companies
    2. Government-linked companies
  - C. India
    1. Family-owned companies
    2. Public sector undertakings
  - D. Singapore
    1. Family-owned companies
    2. Government-linked companies

III. Strategies for regulating extractions of private benefits of control by controlling shareholders are deficient
  - A. Ex ante: Rules on related party transactions (RPTs)
    1. Independent directors'/audit committee opinion or approval
       - i. Independent directors can be removed by controlling shareholders
       - ii. The general meeting and nominating committee are under the control of the controlling shareholders
       - iii. Controlling shareholders exercise significant influence in family-owned companies and state-owned enterprises
       - iv. Independent directors are not necessarily independent from the controlling shareholders
    2. Independent financial adviser opinion
    3. Disinterested shareholders' approval
    4. RPTs that are not subject to the listing rules
  - B. Ex ante: Participative mechanisms
  - C. Ex post: Controlling shareholders as shadow directors
  - D. Ex post: Controlling shareholders as de facto directors
  - E. Ex post: Bona fide for the benefit of the company as a whole
  - F. Ex post: Oppression/unfair prejudice

IV. Conflicts of interest and extractions of private benefits of control not regulated by the law
  - A. Category 1: Exercise of voting (i.e. corporate) powers
    1. Appointment and removal of directors
    2. Dictate to or overrule the directors
    3. Directing directors to take action/binding recommendation
    4. Exercise management power
    5. Major transactions
    6. Authorisation and ratification

B. Category 2: Exercise of powers other than by voting
    7. Dividend payouts
    8. Existing business relationships with the company
    9. Exploitation of corporate opportunities
    10. Investments in competing companies

V. Justifications for imposing fiduciary duties on directors should also apply to controlling shareholders

A. Opportunism
B. Information asymmetry
C. Incomplete contracts

In the previous chapter, I have examined the reasons for the current legal position that shareholders are not subject to fiduciary duties and I showed that they are unconvincing. In this chapter, I advance the argument that controlling shareholders in the listed companies in the four common law jurisdictions in Asia – Hong Kong, Malaysia, India and Singapore – should be subject to fiduciary duties. To make this argument, I proceed as follows: I first discuss an aspect of corporate governance to which insufficient attention has been paid: the significant legal powers that are wielded by shareholders of the listed companies in the four common law jurisdictions in Asia (Part I). I then examine the ownership structure of the listed companies in the four countries and the persistent and serious problem of extractions of private benefits of control by controlling shareholders (Part II). Subsequently, I provide three key justifications as to why fiduciary duties should be imposed on controlling shareholders. First, I critically analyse the *ex ante* and *ex post* legal strategies for regulating extractions of private benefits of control by controlling shareholders and I argue that they are all deficient (Part III). Second, I argue that the existing law does not regulate other types of conflicts of interest between the controlling shareholder and the company that can give rise to extractions of private benefits of control (Part IV). The third and final justification is that the rationales for subjecting directors to fiduciary duties should also apply to controlling shareholders in the four countries (Part V).

I. Shareholders wield significant legal powers

An outline of the powers wielded by shareholders in the four common law jurisdictions in Asia serves three purposes: the first is to give force to the intuition that with great power comes great responsibility.[1] If shareholders wield significant powers, which are amplified when they are controlling shareholders, should they not be subject to the duty to exercise them responsibly to advance corporate interest? But shareholders are only subject to minimal common law limitations when they vote. The well-established rule is that shareholders can generally vote as they please with no regard for or even in opposition to the company's interest. The second purpose is to suggest that the focus of corporate governance in common law concentrated ownership jurisdictions in Asia ought to be this: in light of the significant powers wielded by shareholders, and in view of the risk that controlling shareholders could exercise these powers to benefit themselves at the company's expense, and given the deficient strategies to regulate such conflicts of interest, the question is what legal duties should be imposed on these shareholders. Third and finally, the powers of shareholders have an important bearing on the question of when a fiduciary relationship arises which is analysed in Chapter 5: on one view, it arises when one party (the fiduciary) exercises discretionary powers that impact upon the interests of the other (the beneficiary). Given that courts have justified their imposition of fiduciary duties on this view, a claimant who wants to persuade courts to impose fiduciary duties on controlling shareholders has to first understand the powers wielded by shareholders.

[1] The Parliamentary Debates (Authorised Edition), Fourth Series, First Session of the Twenty-Eighth Parliament of the United Kingdom of Great Britain and Ireland, Volume 152 (First Volume of Session), Commons, Speaker: Winston Churchill, Date: February 28, 1906.

The powers wielded by shareholders in the four common law jurisdictions in Asia include the following:

- Appoint and re-appoint directors, as well as dismiss directors at any time without cause (despite anything in the company's constitution or any agreement between the company and directors)
- Alter the company's constitution
- Requisition general meetings
- Call general meetings (without asking directors to do so)
- Direct directors to take or refrain from taking certain action
- Dictate to or overrule the directors by altering the constitution[2]
- Exercise management power (if provided for in the constitution or statute)
- Authorise or ratify breaches of duties by directors
- Approve executive compensation
- Approve mergers
- Approve significant transactions
- Approve related parted transactions
- Approve loan transactions between the company and directors
- Alter company's status from public to private status
- Issue shares
- Reduce share capital
- Share repurchase

[2] *Bamford v Bamford* [1970] Ch 212, 220; *Automatic Self-Cleansing Filter Syndicate Co Ltd v Cuninghame* [1906] 2 Ch 34, 38; Singapore Companies Act (Cap 50) (revised edn 2006) (SG CA), s 157A(2); HK Model Articles, arts 2(1), 2(2); Hong Kong Companies Ordinance (Cap 622) (HK CO), s 116(2). But note that the alteration does not invalidate any prior acts of the directors that would have been valid had the alteration not been made: HK Model Articles, art 2(2); Malaysia Companies Act 2016 (Act 777) (MY CA), ss 36(1), 36(2) and 211(2). Note that a special resolution is needed to alter the company's constitution and the board of directors' powers is subject to the limitation of the constitution and its modification; India Companies Act 2013 (IN CA), ss 13, 14 and 179 (1).

- Alter class rights attached to shares
- Appoint company's auditor
- Wind up company
- Inspect documents
- Derivative action
- Oppression/unfair prejudice

Table 1 documents in detail the powers conferred on shareholders in the four common law jurisdictions in Asia. These powers may be categorised into two types: corporate powers and non-corporate powers. Corporate powers are exercised on behalf of the company, the result of which is that the decision binds the company and alters its legal position. Examples include appointing and dismissing directors; altering the company's constitution; directing directors to take or refrain from taking certain action; dictating to or overruling the directors by altering the constitution; exercising management power (if provided for in the constitution or statute); authorising or ratifying breaches of duties by directors; approving executive compensation; approving mergers; approving significant transactions; approving related parted transactions; approving loan transactions between the company and directors; altering the status of a company from public to private; and appointing the company's auditor. However, when shareholders exercise non-corporate powers, they do not do so on the company's behalf and their decision does not alter the legal position of the company. Non-corporate powers pertain to intra-shareholder matters (such as altering class rights attached to shares) or rights that are conferred on shareholders in their individual capacities (such as inspection of documents and oppression/unfair prejudice petitions).

Apart from the procedural requirements stipulated in the statute, the company's constitution and listing rules (such as whether ordinary or special shareholder resolution is needed and the notice requirements), the common law restrictions on shareholders' ability to exercise corporate powers are exceptional[3], as they encroach on the well-established principle that shareholders can vote they please, with no regard for or even in opposition to corporate interest.

Thus, subject to any procedural requirements, most of the powers can be exercised by shareholders as they please. Thus, for example, shareholders can dismiss or refuse to reappoint directors who defy their wishes. Shareholders are generally not barred from authorising conflicts of interest between the company and directors (who could be their associates, nominees or even themselves) in order to advance their own interests. Shareholders can approve significant transactions (including but not limited to causing the company to: sell its assets, act as a creditor or guarantor, or enter into other kinds of transactions) in order to benefit themselves at the company's expense. Shareholders can approve in an ordinary resolution extravagant compensation package for the directors (who could be their associates, nominees or the shareholders themselves). Finally, as for related party transactions that are outside the scope of the listing rules, a shareholder who is a party to the transaction can vote in the general meeting to approve the transaction for his own benefit. The duties imposed on directors such as to act in good faith in the company's best interests, to act for proper purposes, or to avoid conflicts of interests, generally do not apply to shareholders.

[3] The most prominent restriction is that shareholders have to act bona fide for the benefit of the company as a whole when they alter the company's constitution (*Allen v Gold Reefs of West Africa Ltd* [1900] 1 Ch 656) and for the benefit of the class a whole when they alter class rights (*British America Nickel Corpn Ltd v O'Brien* [1927] AC 369). But this restriction can be easily overcome as shareholders only need to give a rational/plausible reason for their decision: *Shuttleworth v Cox Bros & Co (Maidenhead) Ltd* [1927] 2 KB 9, 18; David Kershaw, *Company Law in Context: Text and Materials* (2nd edn, OUP 2012) 658. Courts will not decide whether in their view the decision was in fact made in the company's best interests: *Sidebottom v Kershaw, Leese and Company Ltd* [1920] 1 Ch 154, 165-166. The other restriction relates to ratification of breaches of director's duties: for example, shareholders cannot ratify acts that violate the capital maintenance rule (*Trevor v Whitworth* (1887) 12 App Cas 409) or which amounted to a misappropriation of the company's money or property (*Burland v Earle* [1902] AC 83).

If shareholders can exercise these powers for their own benefit at the company's expense, what more in the case of controlling shareholders in concentrated ownership jurisdictions.[4] In the next section (Part II), I examine the concentrated ownership structure of the four common law jurisdictions in Asia and provide concrete examples of how controlling shareholders have engaged in extractions of private benefits of control to the detriment of the company.

II. Concentrated ownership and extractions of private benefits of control

In analysing the issue of expropriation by controlling shareholders in common law Asia, we should distinguish between different types of controlling shareholders and different expropriation methods.

To begin, there are different definitions of controlling shareholder. Under the Stock Exchange of Hong Kong and the Bursa Malaysia Mainboard Listing Rules, a controlling shareholder is one who can exercise or control the exercise of 30% or more of the voting power in a general meeting or who can control the composition of a majority of the board of directors of the issuer.[5] Under the Singapore Exchange Mainboard Rules, a controlling shareholder holds

[4] The fact that controlling shareholders in concentrated ownership jurisdictions can exercise the significant powers conferred on them for self-serving reasons at the company's expense underscores a key omission in works that seek to measure the level of shareholder protection. This is because they do not distinguish between dispersed and concentrated ownership jurisdictions and assume that (1) all shareholders have to be protected (and presumably from management); and (2) the more powers that are conferred on shareholders and the easier for shareholders to exercise them, the better it is for financial and economic development. See for eg the "ten-variable shareholder protection index" that is applied to 30 dispersed and concentrated ownership jurisdictions (including Malaysia and India) in Dionysia Katelouzou and Mathias Siems, 'Disappearing Paradigms in Shareholder Protection: Leximetric Evidence for 30 Countries, 1900-2013' (2015) 15 *Journal of Corporate Law Studies* 127, 130-1.

[5] HKEX listing rule (HKEX LR) chapter 1, para 1.01; Bursa Malaysia Main Market Listing Requirements (Bursa Malaysia LR) para 1.01.

15% or more of the issued shares or who in fact exercises control over the company.[6] Indian law does not define who a controlling shareholder is. The closest term to that is a promoter which is defined as 'a person who has control over the affairs of the company, directly or indirectly whether as a shareholder, director or otherwise.'[7]

Concentrated ownership companies can be generally divided into two types: family-owned companies and state-owned enterprises (SOEs)/government-linked companies (GLCs).[8] The means through which controllers extract private benefits of control include but are not limited to related party transactions, executive compensation, pyramiding and cross-holdings.[9]

Family-owned companies, a dominant feature of the listed companies in common law Asia, give rise to several problems.[10] First, appointment of less qualified family members (as compared to outsiders) to important positions in the company. This is because they trust their own kin more than outsiders or they want to benefit their kin. Second, family owners may be less diversified and hence more risk averse. Third, conflicts between the shareholders and

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[6] Singapore Exchange Rulebook, Definitions and Interpretation.

[7] IN CA, s 2(69)(b). See also s 2(1)(e) of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 which defines control as 'the right to appoint majority of the directors or to control the management or policy decisions exercisable by a person or persons acting individually or in concert.'

[8] See generally, Stijn Claessens and others '*Who Controls East Asian Corporations—and the Implications for Legal Reform*' *Public Policy for the Private Sector*; note no. 195. Washington, DC: World Bank, 1999; Stijn Claessens and others, 'The Separation of Ownership and Control in East Asian Corporations' (2000) 58 *Journal of Financial Economics* 81; Stijn Claessens and others, 'Disentangling the Incentive and Entrenchment Effects of Large Shareholdings' (2002) 57 *Journal of Finance* 2741; Richard W Carney and Travers Barclay Child, 'Changes to the Ownership and Control of East Asian Corporations Between 1996 and 2008: The Primacy of Politics' (2013) *Journal of Financial Economics* 494.

[9] Ibid.

[10] See eg, Michael N Young and others 'Corporate Governance in Emerging Economies: A Review of the Principal-Principal Perspective' (2008) 45 *Journal of Management Studies* 196, 203-4; Pursey PMAR Heugens and others, 'Meta-Analysing Ownership Concentration and Firm Performance in Asia: Towards a More Fine-Grained Understanding' (2009) 26 *Asia Pacific Journal of Management* 481, 484-488; Yi Jiang and Mike W Peng, 'Are Family Ownership and Controlling Large Firms Good, Bad or Irrelevant?' (2011) 28 *Asia Pacific Journal of Management* 15. But there is evidence that the equity capitalisation of family-owned business groups has increased in jurisdictions with strong minority protection laws, which suggests that such groups offer important benefits as long as there are strong laws to curb extractions of private benefits of control: Ronald W Masulis and others, 'Ownership and Control in Family Business Groups Around the World' in Jennifer G Hill and Randall S Thomas (eds), *Research Handbook on Shareholder Power* (Edward Elgar 2015) 142.

directors (who are family members) may be more difficult to manage in view of sibling rivalry or succession concerns.

The second largest type of shareholders in common law Asia are the SOEs/GLCs.[11] There are the PRC SOEs in Hong Kong[12], the GLCs in Singapore[13] and Malaysia[14], and the public sector undertakings (PSUs) in India[15]. Such companies generally pose five risks.[16] First, SOEs/GLCs are likely to have political and social objectives such as equitable distribution and societal welfare that compete or conflict with the commercial objectives of the company which include profit-maximisation. Second, directorial and senior management appointments could be politically motivated or influenced by nepotism and cronyism. Third, given that the government is the investor as well as the regulator, the SOEs/GLCs could be subject to less accountability. Fourth, controlling shareholders not only extract financial gains from the company, but also other kinds of gains such as political connection, prestige, and those deriving from corruption. The result is that SOEs/GLCs are generally less efficient as they engage in strategies that further political and personal agenda to the detriment of the company (and minority shareholders).

[11] Note that while the focus in this chapter is on the government as a controlling shareholder, the government can also act as a minority shareholder, from which conflicts of interest and extractions of private benefits of control can also arise. This will be briefly mentioned in Chapter 7.

[12] See eg, Lin Lin-Wen and Curtis J Milhaupt 'We Are the (National) Champions: Understanding the Mechanisms of State Capitalism in China' (2013) 65 *Stanford Law Review* 697.

[13] See eg, Cheng-Han Tan and others, 'State-Owned Enterprises in Singapore: Historical Insights into a Potential Model for Reform' (2015) 28 *Columbia Journal of Asian Law* 61.

[14] See eg, On Kit Tam and Monica Guo-Sze Tan, 'Ownership, Governance and Firm Performance in Malaysia' (2007) 15 *Corporate Governance: An International Review* 208.

[15] See eg, Jayati Sarkar and Subrata Sarkar, *Corporate Governance in India* (Sage 2012) 91-97.

[16] See eg, Andrei Shleifer and Robert W Vishny, *The Grabbing Hand: Government Pathologies and Their Cures* (Harvard University Press 2002).

Expropriation by controlling shareholders has been well-documented in Malaysia[17], India[18], and Hong Kong.[19] There is no clear evidence[20] of expropriation by controllers in the listed companies in Singapore but the pervasive concentrated ownership structure of those companies strongly suggests the possibility. The most important manifestation of expropriation is extraction of private benefits of control[21], of which tunneling[22] - the diversion of corporate wealth from the company to the controlling shareholder - is the most pervasive instance. It can take at least three forms. First, controlling shareholders can tunnel - transfer resources from the company to themselves but at the company's expense - through related party transactions such as sale of goods or services and intra-corporate loans that are favourable to the controlling shareholders but detrimental to the company.[23] Second, controlling shareholders who are the directors can tunnel by paying themselves unjustifiably high compensation.[24] Finally, they can engage in pyramiding and cross-holdings which are highly prevalent in the listed companies in the four common law countries in Asia, the result of which is that their voting rights far exceed

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[17] See eg, Simon Johnson and Todd Mitton, 'Cronyism and Capital Controls: Evidence from Malaysia' (2003) 67 *Journal of Financial Economics* 351; Ferdinand A Gul, 'Auditors' Response to Political Connections and Cronyism in Malaysia' (2006) 44 *Journal of Accounting Research* 931.

[18] See eg, Marianne Bertrand and others, 'Ferreting Out Tunneling: An Application to Indian Business Groups' (2002) 117 *Quarterly Journal of Economics* 121; Raja Kali and Jayati Sarkar, 'Diversification and Tunneling: Evidence from Indian Business Groups' (2011) 39 *Journal of Comparative Economics* 349.

[19] See eg, Yan-Leung Cheung and others, 'Tunnelling, Propping, and Expropriation: Evidence from Connected Party Transactions in Hong Kong' (2006) 82 *Journal of Financial Economics* 343.

[20] In one study, the authors used related party transactions in the listed companies in Singapore as a proxy for tunneling: see Agung Juliarto and others, 'Managerial Ownership Influencing Tunnelling Behaviour' (2013) 7 *Australasian Accounting Business & Finance Journal* 1, 12-13.

[21] Ronald J Gilson and Alan Schwartz, 'Constraints on Private Benefits of Control: Ex Ante Control Mechanisms versus Ex Post Transaction Review' (2013) *Journal of Institutional and Theoretical Economics* 160, 161-2; Ronald J Gilson, 'Controlling Shareholders and Corporate Governance: Complicating the Comparative Taxonomy' (2006) 119 *Harvard Law Review* 1641, 1651; Alexander Dyck and Luigi Zingales, 'Private Benefits of Control: An International Comparison' (2004) 59 *Journal of Finance* 537.

[22]Simon Johnson and others, 'Tunneling' (2000) 90 *American Economic Review* 22.

[23] See eg, Simeon Djankov and others, 'The Law and Economics of Self-Dealing' (2008) 88 *Journal of Financial Economics* 430.

[24] See eg, Yan-Leung Cheung and others, 'Ownership Concentration and Executive Compensation in Closely Held Firms: Evidence from Hong Kong' (2005) 12 *Journal of Empirical Finance* 511.

their cash flow rights.[25] Pyramiding, in brief, refers to the practice of deriving more benefits than what the person's share of equity ownership would ordinarily provide by having a controlling stake in a parent company which in turn controls other companies. Suppose a family owns a group of companies. The family owns 100% of company A which in turn owns 51% of company B which in turn owns 51% of company C. The family ends up controlling with as little as 10% of shares in company C. Thus, the family has control rights in company C far in excess of its cash flow rights. The family can therefore transfer resources from company C to company A (where it has higher cash flow rights)[26] through, for example, related party transactions.

That said, controlling shareholders and group companies are not always or necessarily a bad thing.[27] They can more effectively and efficiently monitor and discipline management than dispersed shareholders. This is because they have more incentives and legal powers as they have greater investments at stake and greater voting rights. Further, unlike dispersed shareholders, they do not suffer from collective action problems. Coordinating with other shareholders becomes easier and cheaper because, among other reasons, they have better access to information. Controlling shareholders are also more likely to be committed to the company, particularly if they have long term contracts with the company, and in the case of family-owned companies, they would want their family members and descendants to inherit the business.

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[25] Stijn Claessens and others, 'The Separation of Ownership and Control in East Asian Corporations' (2008) 58 *Journal of Financial Economics* 81, 91; Heitor V Almeida and Daniel Wolfenzon, 'A Theory of Pyramidal Ownership and Family Business Groups' (2006) 61 *Journal of Finance* 2637; Ronald W Masulis and others, 'Ownership and Control in Family Business Groups Around the World' in Jennifer G Hill and Randall S Thomas (eds), *Research Handbook on Shareholder Power* (Edward Elgar 2015) 142, 150-1.

[26] See eg, Sarkar and Sarkar (n 15) 9.

[27] See eg, Michael N Young and others '*Corporate Governance in Emerging Economies: A Review of the Principal-Principal Perspective'* (2008) 45 *Journal of Management Studies* 196, 203-4; Albert Choi, 'Concentrated Ownership and Long-Term Shareholder Value' (2018) 8 *Harvard Business Law Review* (forthcoming). There are studies that suggest that there is a correlation between family-owned companies in developing economies and better corporate performance: Tarun Khanna and Krishna Palepu, 'Is Group Affiliation Profitable in Emerging Markets? An Analysis of Diversified Indian Business Groups' (2000) 55 *Journal of Finance* 867; Tarun Khanna and Jan W Rivkin, 'Estimating the Performance Effects of Business Groups in Emerging Markets' (2000) 22 *Strategic Management Journal* 45.

Further, controlling shareholders are more likely to remain in the company for the long-term and hence they would be concerned about the company's long-term performance because private benefits of control create a lock-in effect as they are private and non-transferrable. Additionally, in emerging economies with underdeveloped institutions (such as capital markets, law enforcement regimes, takeover markets and effective boards), controlling shareholders may act as viable substitutes by providing the necessary capital and by being effective monitors of management and hence reducing managerial opportunism and short-termism.[28]

Moreover, there are advantages with the government as a controlling shareholder in listed SOEs.[29] The government can continue to pursue social welfare objectives that can benefit the economy and society while balancing it with the need to pursue profit-oriented goals (the latter of which are likely to be the result of pressure from private shareholders). It can also eschew short-termism and take a long-term perspective, while being subject to disciplinary pressure of the stock price. It can enhance its reputation and efficiency due to increased transparency and accountability (as a result of being subject to the listing rules on corporate governance, disclosure and accounting).

Finally, the most common mechanism through which controlling shareholders (whether family members or governments) engage in tunneling – related party transactions – is not necessarily a bad thing; RPTs can be value-enhancing under certain circumstances, such as when a company cannot obtain the desired financing from external sources or when the

[28] See eg, Ronald J Gilson, 'Controlling Family Shareholders in Developing Countries: Anchoring Relational Exchange' (2007) 60 *Stanford Law Review* 633; Raymond Fisman and Tarun Khanna, 'Facilitating Development: The Role of Business Groups' (2004) 32 *World Development* 609; Ravi Dharwadkar and others, 'Privatization in Emerging Economies: An Agency Theory Perspective' (2000) 25 *Academy of Management Review* 650.

[29] Mariana Pargendler and others, 'The Puzzle of Private Investment in State Controlled Firms', Harvard Business School WP 13-071 (2013) <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2217627> accessed 1 December 2018; Mary Shirley and John Nellis, *Public Enterprise Reform: The Lessons of Experience*, 1991, Washington, DC: Economic Development Institute of the World Bank.

company requires certain expertise for the development of its business and the controlling shareholder is able to provide the financing and expertise.[30]

With the above general analysis in mind, I shall now provide a specific analysis of the nature of concentrated ownership structure and its attendant problems in each of the four common law jurisdictions in Asia.

A. Hong Kong

The listed companies in Hong Kong are dominated by controlling shareholders, specifically families and the PRC government. One influential study found that blockholders hold an average of 28.08% of shares.[31] Moreover, it was found that in 69% of the listed companies, the single ultimate owners hold 90% or more of the shares.[32] There is also evidence of pervasive expropriation by the controlling shareholders.

1. Family-owned companies

[30] See eg, Luca Enriques, 'Related Party Transactions' in Jeffrey N Gordon and Wolf-Georg Ringe (eds), *The Oxford Handbook of Corporate Law and Governance* (OUP 2015) 4; Vladimir A Atanasov and others, 'Unbundling and Measuring Tunneling' (2014) University of Illinois Law Review 101, 108.

[31] Stijn Claessens and others, 'The Separation of Ownership and Control in East Asian Corporations' (2000) 58 *Journal of Financial Economics* 92, 99.

[32] Ibid 92.

One study found that families who have at least 20% of the voting rights own 72.5% of the largest listed companies.[33] The top 15 families who operate businesses in Hong Kong control assets that amount to 84% of Hong Kong's GDP.[34] A more recent study found that family-owned companies consist of 75.6% of all the listed companies in Hong Kong and 81% of these family-owned companies have families who possess at least 30% of the voting rights.[35] Family-owned companies will continue to remain concentrated.[36] One study showed that the change in year-to-year absolute percentage in family ownership is less than 10% for more than 75% of the listed family-owned companies.[37]

Family members play an important role in the management of the company. A recent study stated that the family members comprise 17.4% of board members in family-owned companies.[38] In 60% of the family-owned companies, the CEO and the chair of the board are the same person as compared to 24% of non-family owned companies.[39] Family-owned companies consist of 76.5% of all the companies with CEO-chair duality.[40] Unsurprisingly, the percentage of independent directors in family-owned companies is lower than that of non-family ones. Independent non-executive directors consist of 38.8% of all the board members

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[33] Ibid106

[34] Ibid 108.

[35] Zhilan Chen and others, 'Ownership Concentration, Firm Performance, and Dividend Policy in Hong Kong' (2005) 13 *Pacific-Basin Finance Journal* 431, 436.

[36] David Donald and others, *A Financial Center for Two Empires: Hong Kong's Corporate, Securities and Tax Laws in its Transition from Britain to China* (CUP 2014) 99.

[37] Zhilan Chen (n 35).

[38] Kim Lee and Lisa Barnes, 'Corporate Governance and Performance in Hong Kong Founded Family Firms: Evidence From the Hang Seng Composite Industry Index' (2017) 51 *Journal of Developing Areas* 410, 403.

[39] Tin-Yan Lam and Shu-Kam Lee, 'Family Ownership, Board Committees and Firm Performance: Evidence from Hong Kong' (2012) 12 *Corporate Governance: The International Journal of Business in Society* 353, 358.

[40] Chen (n 35).

in family-owned companies.[41] The percentage in which more than one third of the board consists of independent directors in family-owned companies is 60.5 as compared to 65.3 in non-family owned companies.[42] Controlling families perceive non-independent directors as a threat to their authority and disruptive to the decision-making process.[43]

There is ample evidence of expropriation in family-owned companies. It takes at least three forms. First, controlling shareholders in intra-group companies can prop up a financially distressed company by transferring assets or cash – a prime instance of related party transaction – from a financially healthy company to the distressed company to the detriment of the healthy company and its shareholders.[44] They can also prop up by causing part of the retained earnings of the healthy company to be channelled to the distressed company; this would mean less cash for the healthy company to pursue investments or R&D opportunities, to the detriment of the healthy company.[45] Second, controlling shareholders who are board members, or who can influence the directors, can cause the board to declare huge dividend payouts.[46] The payouts are substantial. For example, the ratio of dividend payout to cash compensation for CEO who is also the chairman is 14:1.[47] And the ratio for the average chairman is 18:1.[48] The evidence shows that the substantial payouts reflect huge extraction of company's resources to the benefit

[41] Sidney Leung and others, 'Corporate Board and Board Committee Independence, Firm Performance, and Family Ownership Concentration: An Analysis Based on Hong Kong Firms' (2014) 10 *Journal of Contemporary Accounting & Economics* 16, 26.

[42] Ibid at 24.

[43] Ibid at 17.

[44] Yan-Leung Cheung and others, 'Board Structure and Intragroup Propping: Evidence from Family Business Groups in Hong Kong' (2014) 43 *Financial Management* 569, 569-601.

[45] Ibid 569-570.

[46] Chen (n 35).

[47] Ibid.

[48] Ibid.

of the controlling shareholders.[49] Third, insider trading is prevalent in family-owned companies.[50] A study found that executives may be strongly incentivised to pursue earnings management to increase their private benefits including insider trading.[51] A more recent study found that executives who are linked to the controlling shareholders are motivated to pursue earnings management by adjusting the reported earnings upwards.[52] This is to signal that the company is doing well which will translate into an increase in share price, and this in turn will allow the executives to sell their shares at a higher price. There is a strong correlation between earnings management and insider trading after the fiscal year end.[53]

2. State-owned enterprises

The other type of controlling shareholder that has a pervasive and vital influence in Hong Kong is the PRC government who has direct or indirect ownership of the SOEs listed in Hong Kong.[54] The PRC government delegates authority to the State-Owned Assets Supervision and Administration Commission (SASAC) to exercise the powers and discharge

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[49] Ibid 445.

[50] Bikki Jaggi and Judy Tsui, 'Insider Trading, Earnings Management and Corporate Governance: Empirical Evidence Based on Hong Kong Firms' (2007) 18 *Journal of International Financial Management & Accounting* 192, 213.

[51] Joseph PH Fan and TJ Wong, 'Corporate Ownership Structure and the Informativeness of Accounting Earnings in East Asia' (2002) 33 *Journal of Accounting and Economics* 401.

[52] Bikki Jaggi and Judy Tsui, 'Insider Trading, Earnings Management and Corporate Governance: Empirical Evidence Based on Hong Kong Firms' (2007) 18 *Journal of International Financial Management & Accounting* 192, 213.

[53] Ibid 200.

[54] Donald (n 36) 228-229.

the duties as a controlling shareholder. The listed SOEs come in two types.[55] H-shares companies are incorporated in China, and are listed on one of the stock exchanges in China but are also cross-listed in Hong Kong. Red chip companies however are incorporated outside China and Hong Kong but are listed in Hong Kong. SOEs constitute about 20.1% of the listed companies in Hong Kong, including 11 out of the top 30 companies by market capitalisation.[56] All the SOEs account for 40% of total market capitalisation of listed companies on the Main Board of the Stock Exchange of Hong Kong (SEHK).[57]

Given that the PRC government is the controlling shareholder in the SOEs, it appoints the management who are affiliated with the state.[58] The management in turn enjoy political benefits such as promotion to senior government positions in China.[59] It is not surprising that there is evidence of expropriation in SOEs by the controlling shareholder. In a widely cited study, it was found that as compared to family-owned companies, there is a higher frequency of value destroying related party transactions undertaken in SOEs, which resulted in negative and significantly lower abnormal returns.[60] These related party transactions include but are not limited to asset acquisitions by the listed company from the controlling shareholder (or a company affiliated with it), sale of goods and services between the listed company and the controlling shareholder (or its affiliated company), and cash payments from the listed company

55 Ibid.

56 HKEX Mutual Market, Listed Companies, Stock Lookup <https://www.hkex.com.hk/eng/csm/result.htm?location=companySearch&SearchMethod=2&mkt=hk&LangCode=en&StockType=ALL&Ranking=ByMC&x=33&y=14> accessed 1 December 2018.

57 HKEX China Dimension <https://www.hkex.com.hk/eng/stat/smstat/chidimen/cd_mc.htm> accessed 1 December 2018.

58 Mingyi Hung and others, 'Political Considerations in the Decision of Chinese SOEs to List in Hong Kong' (2012) 53 *Journal of Accounting and Economics* 435, 439.

59 Ibid 447.

60 Cheung (n 19) 372.

to the controlling shareholder (or a company affiliated with it), or cash guarantees by the listed company for the debts owed by the controlling shareholder (or its affiliated company).[61] Further, H-shares and Red Chips companies are more likely to enter into transactions that violate SEHK's listing rules and exhibit poor information disclosure.[62]

Further, the state as the controlling shareholder of H-share companies uses these companies as a tool to advance its political or socio-economic agendas with little regard for the long term commercial success of the companies.[63] One consequence is asset stripping in, and poor performance by, these companies.[64] In sum, the SOEs listed in Hong Kong are not commercially driven and are highly susceptible to political influence from its controlling shareholder.[65] Unsurprisingly, a study found that investors discount SOEs and they are traded at lower valuation on the SEHK.[66] Another study also found that H-share companies generally become less profitable in terms of return of equity and return of assets after they have been listed on the SEHK.[67]

B. Malaysia

[61] Ibid 356.

[62] Ibid 375.

[63] Shu-Yun Ma, 'Role of the State in Chinese Enterprises Listed in Hong Kong' (2002) 15 *Pacific Review* 279.

[64] Ibid.

[65] Curtis J Milhaupt, 'Chinese Corporate Capitalism in Comparative Context' in Weitseng Chen (ed), *The Beijing Consensus? How China Has Changed the Western Ideas of Law and Economic Development* (CUP 2017) Ch 11.

[66] Yan-Leung Cheung and others, 'Does Corporate Governance Predict Future Performance? Evidence from Hong Kong' (2011) 40 *Financial Management* 159.

[67] Guihai Huang and Frank M Song, 'The Financial and Operating Performance of China's Newly Listed H-Firms' (2005) 13 *Pacific-Basin Finance Journal* 53, 73.

Concentrated ownership is the norm in listed companies in Malaysia. One study found that 38% of the 50 largest listed companies by market capitalisation in Malaysia have one dominant shareholder (who holds more than 40% control); 85% of these 50 companies are GLCs and 15% are family-owned companies.[68] A more recent study that covers data from 2002-2011 has found that the five largest shareholders hold an average of 70% of the shares.[69]

1. Family-owned companies

Family-owned companies constitute about one third of the listed companies in Malaysia and they have an average of RM1,700 million worth of assets.[70] Up to 57% of the top 100 listed companies are owned by families and they own 20% or more of the shares through their family members.[71] In a more extensive study, it was found that 39% of 793 listed companies consist of family members who are the top 30 largest shareholders.[72]

Family members play a crucial role in the governance of the family-owned companies. Approximately 63% of the listed companies controlled by business families have at least two

[68] Shanthy Rachagan and Aiman Nariman Mohd Sulaiman, 'Controlling Shareholders: Issues and Challenges for Shareholders' Empowerment in Directors' Remuneration in Corporate Malaysia' (2013) 9 *Asian Journal of Comparative Law* 267, 276.

[69] Hooi Hooi Lean and others, 'Ownership Concentration, Family Ownership and Leverage: Evidence from Malaysia' (2015) 52 *Malaysian Journal of Economic Studies* 117.

[70] Haslindar Ibrahim and Fazilah Abdul Samad, 'Corporate Governance Mechanisms and Performance of Public-Listed Family-Ownership in Malaysia' (2011) 3 *International Journal of Economics and Finance* 105.

[71] Sin Huei Ng and others, 'Factors Influencing the Performance of Family-Controlled Publicly-Listed Firms in Malaysia' (2012) 1 *Review of Integrative Business and Economics Research* 179.

[72] Lean (n 69).

family members in leadership positions.[73] 30.6% of the top 150 listed companies have CEOs who are also the chair persons.[74] Among the listed companies with CEO-chair duality, family-owned companies constitute 90.9%.[75] Thus, family members wield significant powers because in addition to their voting powers, they also wield management powers.

There is evidence of tunneling. A study of 141 family-owned companies in the Malaysian manufacturing sector found that excess control rights (i.e. the difference between voting rights and cash flow rights held by the family controlling shareholders as a result of pyramiding) provide more incentives to the family controllers to extract private benefits of control.[76] In another study of 191 listed companies where the controlling shareholders are also executive directors, it was found that when controllers hold between 23% to 75% of shares, a unit increase in ownership results in about 0.8% increase in salary; in short, once the controlling shareholders who are directors own a certain amount of shares, they will pay themselves excessive salary to the detriment of the company and minority shareholders.[77] In another study, it was found that controlling shareholders tunnel through related party transactions.[78]

[73] Muraddin Bin Purag and others, 'Corporate Governance and Capital Structure of Malaysian Family-Owned Companies' (2016) 11 *Journal of Business & Retail Management Research* 18.

[74] Tam and Tan (n 14).

[75] Ibid.

[76] Chin Fei Goh and others, 'Economic Incentives for Family Controlling Shareholders and the Monitoring Role of Non-Dominant Large Shareholders in Corporate Governance: Evidence from the Manufacturing Firms in Malaysia' (2014) 17 *South African Journal of Economic and Management Sciences* 471.

[77] Boon Leong Lim and Siew Hwa Yen, 'Agency Problem and Expropriation of Minority Shareholders' (2011) 48 *Malaysian Journal of Economic Studies* 37, 53; Syaiful Baharee Jaafar and others, 'Remuneration Committee and Director Remuneration in Family-Owned Companies: Evidence from Malaysia' (2012) 8 *International Review of Business Research Papers* 17.

[78] Nurul Huda Mustafa and others, 'Expropriation of Minority Shareholders' Rights: Evidence from Malaysia' (2011) 2 *International Journal of Business and Social Science* 215.

2. Government-linked companies

The term government-linked companies (GLCs) in essence refers to companies in which the Malaysian government has a controlling stake. Specifically, GLCs are defined in two main ways.[79] The first refers to companies that the Malaysian government exercises control directly through incorporated companies consisting of Kumpulan Wang Persaraan (KWAP), Khazanah Nasional Bhd (Khazanah), Minister of Finance (Incorporated) and the Central Bank of Malaysia.[80] Thus, the controlling shareholders of the GLCs are these four entities, and the ultimate controller is the government. The second refers to companies whose controlling shareholders are the government-linked investment companies (GLICs) consisting of the Employees Provident Fund (EPF), Permodalan Nasional Bhd (PNB), Lembaga Tabung Haji (LTH), Khazanah, and Lembaga Tabung Angkatan Tentera (LTAT). Among the 30 largest listed companies in Malaysia, GLCs consist of 12 companies, and there are 6 GLCs among the top 10 largest companies.[81] Among all the companies, GLCs have the most concentrated shareholding structure.[82] A study of the top 150 listed companies by market capitalisation found that the government holds an average of 55.23% of the shares in GLCs.[83] Although the

[79] CG Work Team for the Government Linked Companies Transformation Program, FAQs, What are GLC and GLIC? <http://www.pcg.gov.my/faqs#> accessed 1 December 2018.

[80] The objective of KWAP is to manage retirement funds of civil servants. Khazanah is the investment arm of the government to hold and manage the government's assets. Minister of Finance Incorporated is the body corporate under the Minister of Finance.

[81] Michael Carney and Edo Andriesse, 'Malaysia: Personal Capitalism' in Michael A Witt and Gordon Redding (eds), *The Oxford Handbook of Asian Business Systems* (OUP 2014) 151.

[82] Shanthy Rachagan and Aiman Nariman Mohd Sulaiman, 'Controlling Shareholders: Issues and Challenges for Shareholders' Empowerment in Directors' Remuneration in Corporate Malaysia' (2013) 9 *Asian Journal of Comparative Law* 267.

[83] Tam and Tan (n 14).

government's share fell to 44% in 2012, the government still maintains its controlling stake in the GLCs.[84]

Although GLCs in Malaysia are given preferential treatment in terms of business opportunities and access to capital, they generally underperform non-GLCs in terms of market performance and investment returns.[85] This is consistent with prior research on the performance of state-owned companies, but is at odds with the GLCs in Singapore (discussed below) which exhibit better performance than non-GLCs.[86] Importantly, GLCs in Malaysia are more vulnerable to extractions of private benefits of control by the controlling shareholders.[87] The lacklustre performance of GLCs and the presence of tunnelling are due to several reasons. A key purpose of the government's investments in, and creation of, GLCs is to engage in affirmative action to protect and promote the interests of Muslim Malays instead of pursuing commercial profitability and competitiveness.[88] As a result, the GLCs are generally immune from market discipline as they are protected by the government.[89] Further, most GLCs are managed by civil servants who do not have the requisite expertise. Also, it has been said that

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[84] Hooi Hooi Lean and others, 'Ownership Concentration, Family Ownership and Leverage: Evidence from Malaysia' (2015) 52 *Malaysian Journal of Economic Studies* 117.

[85] Nazrul Hisyam Ab Razak and others, 'Do Government Linked Companies (GLCs) Perform Better than Non-GLCs?' (2011) 1 *Journal of Applied Finance & Banking* 213; Nurul Afzan Najid and Rashidah Abdul Rahman, 'Government Ownership and Performance of Malaysian Government-Linked Companies' (2011) 61 *International Research Journal of Finance and Economics* 42.

[86] James S Ang and David K Ding, 'Government Ownership and the Performance of Government-Linked Companies: The Case of Singapore' (2006) 16 *Journal of Multinational Financial Management* 64.

[87] Simon Johnson and Todd Mitton, 'Cronyism and Capital Controls: Evidence from Malaysia' (2003) 67 *Journal of Financial Economics* 351; Puan Yatim and others, 'Governance Structures, Ethnicity, and Audit Fees of Malaysian Listed Firms' (2006) 21 *Managerial Auditing Journal* 757; Ferdinand A Gul, 'Auditors' Response to Political Connections and Cronyism in Malaysia' (2006) 44 *Journal of Accounting Research* 931.

[88] Carney and Andriesse (n 81) 146-150.

[89] Takashi Torii, 'The New Economic Policy and the United Malays National Organisation, with Special Reference to the Restructuring of the Malaysian Society' (2007) 35 *Developing Economies* 209; AB Shamsul, 'The Economic Dimension of Malay Nationalism – The Socio-Historical Roots of the New Economic Policy and Its Contemporary Implications' (1997) 35 *Developing Economies* 240; Pek Koon Heng, 'The New Economic Policy and the Chinese Community in Peninsula Malaysia' (1997) 35 *Developing Economies* 262.

politicians use the GLCs as a tool to advance their own personal and political agenda, and the board and management of the GLCs are expected to do their bidding.[90] This is not surprising as the GLCs depend on political patronage for their success.[91]

It would be remiss not to briefly mention the most explosive case of corruption involving 1MDB, a GLC and a sovereign wealth fund. There have been numerous allegations of egregious corruption made against 1MDB, which is under investigation by authorities in the US, UK, Singapore, Hong Kong and Australia.[92] The main allegation is that money was siphoned off from 1MDB to the personal accounts of the former Malaysian Prime Minister Najib Razak and his allies.

C. India

A 2006 research showed that 92.8% of the companies consist of concentrated ownership.[93] Among the top 20 companies by market capitalisation, promoters i.e. persons who have effective control over a listed company, consist of 59.32% and non-promoters which consist mainly of financial institutions, 13.76%.[94] Based on a research of 3155 listed companies from 2007 to 2008, promoters held the biggest block, ranging between 46% to 62%.[95] Outsiders

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[90] Edmund Terence Gomez and KS Jomo, *Malaysia's Political Economy, Politics, Patronage and Profits* (2nd edn, CUP 1999).

[91] Carney and Andriesse (n 81) 150.

[92] The most comprehensive analysis to date can be found in Wall Street Journal <http://www.wsj.com/specialcoverage/malaysia-controversy> accessed 1 December 2018.

[93] Sarkar and Sarkar (n 15) 93.

[94] Ibid 96.

[95] Ibid 94.

constituted less than 10% on average.[96] About 20 out of the 32 companies (62.5%) had an increase in promoter ownership from 2006 to 2013.[97] Further, two-thirds of the 18 recent entrants to the Nifty have controlling interests that exceed 50%.[98] Thus, concentrated ownership has remained and will remain a central feature of the listed companies in India.

Empirical evidence shows that controlling shareholders often manage the companies they own. Using information on the Nifty, a leading index of 50 companies on the National Stock Exchange of India, a recent research found that in about 33 out of the 50 companies (40%), shareholders hold management positions in the company.[99] There is evidence of widespread tunneling.[100]

1. Family-owned companies

A 2011 study of 2568 listed family businesses in ten Asian countries found that India has the highest percentage of family businesses (67%).[101] The study also found that out of the 983 listed Indian companies, 663 are family businesses which accounted for 46.8% of market capitalisation. Family companies also consist of the bulk of the promoters in listed companies.

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[96] Ibid 95.

[97] George S Geis, 'Shareholder Power in India' in Jennifer G Hill and Randall S Thomas (eds), *Research Handbook on Shareholder Power* (Edward Elgar 2015) 599-600.

[98] Ibid 600.

[99] Ibid 598.

[100] Marianne Bertrand and others, 'Ferreting Out Tunneling: An Application to Indian Business Groups' (2002) 17 *Quarterly Journal of Economics* 121.

[101] Credit Suisse - Asian Family Businesses Report 2011: Key Trends, Economic Contribution and Performance.

Promoters include group affiliates and standalones. Group affiliates consist of 50.15%, of which 12.67% are families.[102] Standalone companies consist of 45.98%, of which families consist of 29.68%.[103]

Controlling family companies own an average of 53.2% of shares as found in a study of the top 500 companies listed on the Bombay Stock Exchange.[104]. This figure is unlikely to vary significantly in the future given that there was little change in the ownership structure from 2006 to 2010 despite the global financial crisis in 2009.[105]

In light of their ownership, it is not surprising that controlling families have control over the appointment of board members and senior management. For example, the chair and CEO who are family members or affiliated with the controlling family account for 73% and 90%, respectively of the listed companies.[106] In 38.5% of family firms, the chair and the CEO are one and the same, as compared to 30.9% in non-family firms. Further, the CEO who are family members have owned and managed about 33% of the top 300 family-owned listed companies.[107].

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[102] Sarkar and Sarkar (n 15) 94.

[103] Ibid.

[104] Rakesh Pandey, 'Effects of Controlling Family Status, Family-Impacted Governance and Top Management Characteristics on Financial and Social Performance of Listed Companies in India' (2012) Doctor of Philosophy (PhD), Accounting, RMIT University 141.

[105] Shireenjit Johl and others, 'Family Generation, Leadership and Performance: The Role of Outside Directors in Indian Family Firms' (2010) 8 *Corporate Ownership and Control* 646; Rakesh Pandey and others, 'Governance of Large Family Companies in Traditional and New Economy Industries in India: Effects on Financial Performance' (2011) 8 *Corporate Ownership and Control* 108.

[106] Rakesh Pandey, 'Effects of Controlling Family Status, Family-Impacted Governance and Top Management Characteristics on Financial and Social Performance of Listed Companies in India' (2012) Doctor of Philosophy (PhD), Accounting, RMIT University 142.

[107] Ibid 141.

Moreover, the CEO and chair who are from the founder family accounted for 67% of the family-owned companies.[108] And about 26.81% of directors come from founder families.[109] More recently, it was found that 65.5% of the directors in family-owned firms are from founder families.[110] The same study found that the founder family director who is also the CEO accounts for 77% of family companies.[111] In sum, the board and senior management are dominated by founder-family members.

Extraction of private benefits of control is a common phenomenon among family-owned companies.[112] There is evidence of: tunneling using pyramiding[113] and related party transactions[114], earnings management where the controlling shareholders distort the financial performance of company for personal gains, falsification of accounts, siphoning of funds, and improper invoicing.[115]

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[108] Ibid 143.

[109] Ibid.

[110] Melvin Jameson and others, 'Controlling Shareholders, Board Structure, and Firm Performance: Evidence from India' (2014) 27 *Journal of Corporate Finance* 1, 7.

[111] Ibid.

[112] See eg Sarkar and Sarkar (n 15) 156-163; Malik M Hafeez, 'Domination of Family Owned Corporations and Problems of Corporate Governance in Emerging Markets' (2014) *South East Asia Journal of Contemporary Business, Economics and Law* 9, 14.

[113] See eg, Raja Kalia and Jayati Sarkar, 'Diversification and Tunneling: Evidence from Indian Business Groups' (2011) 39 *Journal of Comparative Economics* 349.

[114] See eg, Jayashree Saha, 'Essays on Related Party Transactions in India', 2006 Draft Ph.D. Thesis, Indira Gandhi Institute of Development Research, Mumbai, India.

[115] Sarkar and Sarkar (n 15) 162-3. The egregious case of Satyam being one such instance: see Afra Afsharipour, 'The Promise and Challenge of India's Corporate Governance Reforms' (2010) 1 *Indian Journal of Law and Economics* 1.

2. Public sector undertakings

State-owned enterprises are known as 'public sector undertakings' (PSUs) in India.[116] The government is the controlling shareholder in the PSUs[117] which include the oil, gas, mining and electricity companies. In one study, while PSUs account for 0.19% of the total companies, they constitute 25% of the paid-up capital, equivalent to 15% of the GDP.[118] In another study, PSUs account for 23% of the market capitalisation.[119]

The government via the administrative ministry wields enormous power over the PSUs through the nomination and appointment of directors (including the independent directors) and other senior management.[120] Further, the government, not the board, makes the strategic decisions.[121] The board's role is generally reduced to those of managerial and execution

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[116] The most comprehensive analysis of the state-owned enterprises in India can be found in *State Owned Enterprises in India: Reviewing the Evidence*, OECD Occasional Paper (26 January 2009), <https://www.oecd.org/daf/ca/corporategovernanceofstate-ownedenterprises/42095406.pdf> accessed 1 December 2018.

[117] The PSUs consists of: the Central Public Sector Enterprises where the government of India has control; public sector banks where the central or state (provincial) government owns at least 51%; and the state level public enterprises where the state (provincial) government owns at least 51%. As of 31 March 2016, the Central Government continues to have majority equity holding of 69.15% in CPSEs. See *Public Enterprises Survey 2015-2016* (Department of Public Enterprises, Government of India) 41 <http://dpe.gov.in/sites/default/files/PES_Annual_Report_English.pdf> accessed 1 December 2018

[118] Lawrence Saez, 'India: From Failed Development State Towards Hybrid Market Capitalisation' in Michael A Witt and Gordon Redding (eds), *Oxford Handbook of Asian Business Systems* (OUP 2014) 59.

[119] These PSUs consist of central state-owned enterprises and public sector financial institutions: see *State Owned Enterprises in India: Reviewing the Evidence*, OECD Occasional Paper (26 January 2009) 14.

[120] S Subramanian, 'A Comparison of Corporate Governance Practices in State-Owned Enterprises and Their Private Sector Peers in India' (2016) 5 *IIM Kozhikode Society & Management Review* 200, 204.

[121] Jayanth Rama Varma, 'Corporate Governance in India: Disciplining the Dominant Shareholder' (1997) 9 *IIMB Management Review 5*.

functions.[122] Moreover, similar to family-owned companies, the role of chairman and CEO is not separated in most PSUs.[123]

There is evidence of extractions of private benefits of control by controlling shareholders in PSUs. They include but are not limited to[124] (1) ordering the company to set prices for its goods that are below the market rate; (2) misusing the assets of the company for improper purposes such as using the cash of a coal company to pay for the government's food programmes[125]; and (3) ordering the company to subsidise the activities of other companies. The main reason for expropriation is the conflicting objectives between the government (who has political and personal agendas and plays multiple, competing roles as the regulator and controlling shareholder) and the minority shareholders (who are usually concerned with profit maximisation).[126] On one view, the government uses the PSUs, particularly those that have key strategic or national implications such as those related to public utilities, to advance political objectives including the advancement of social welfare.[127] On another view, the government has been treating the PSUs as cash cows to further their own personal ends to the detriment of the PSUs.[128] The PSUs are not run as arms-length, commercial entities. What facilitated the

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[122] S Subramanian, 'A Comparison of Corporate Governance Practices in State-Owned Enterprises and Their Private Sector Peers in India' (2016) 5 *IIM Kozhikode Society & Management Review* 200, 204.

[123] Ibid 206

[124] R Jagannathan, 'Why Only CIL? Here Are 9 Other PSU Boards Investors Can Sue' *First Post* (20 Dec 2014).

[125] In one egregious example, the Coal Minister said "Cash-rich companies like Coal India Ltd can lend to the government whenever the government is in need of funds. For example, enactment of the food security bill would require huge funds. Coal India belongs to the people of this country and an amount of Rs 25,000 crore can easily be given to the government for implementing social schemes. We, however, have not discussed anything with the finance ministry yet": Sarita Singh and Himangshu Watts, 'Corruption, Inefficiency Eat 25% of CIL output: Sriprakash Jaiswal' *Economic Times* (19 Oct 2011).

[126] YRK Reddy, *The First Principles of Corporate Governance for Public Enterprises in India* (2001) <http://www.academyofcg.org/firstprinciples.htm> accessed 1 December 2018.

[127] Asish K Bhattacharyya, 'Public Enterprises - Corporate Governance and the Role of Government' (March 10, 2005) <https://ssrn.com/abstract=697381 or http://dx.doi.org/10.2139/ssrn.697381> accessed 1 December 2018.

[128] Sushil Khanna, 'The Transformation of India's Public Sector' (2015) 50 *Economic & Political Weekly* 47.

expropriation is that the government, as the controlling shareholder, wields enormous power over the appointment of the directors and senior management. The important decisions are not taken by the board but by the government.[129]

D. Singapore

More than 90% of Singapore's largest 100 listed companies are dominated by controlling shareholders.[130] The two most important types of companies in Singapore are family-owned companies and GLCs. Although there appears to be no empirical study that clearly demonstrates expropriation by controlling shareholders in Singapore[131], the highly concentrated ownership structure, the entrenchment of family members in directorial and managerial positions for long periods of time, and the substantial value of related party transactions, all point toward the possibility of tunneling.

[129] Jayanth Rama Varma, 'Corporate Governance in India: Disciplining the Dominant Shareholder' (1997) 9 *IIMB Management Review* 5.

[130] Luh Luh Lan and Umakanth Varottil, 'Shareholder Empowerment in Controlled Companies: the Case of Singapore' in Jennifer G Hill and Randall S Thomas (eds), *Research Handbook on Shareholder Power* (Edward Elgar 2015) 579.

[131] But note that Singapore GLCs have been guilty of corruption involving bribery to foreign entities: see the GLC Kepple Offshore & Marine (of which Temasek is the ultimate controlling shareholder) which has been fined US$422 million in 2016 for bribing government officials in Brazil in exchange for business deals: <http://www.straitstimes.com/business/companies-markets/elaborate-scheme-used-to-disguise-bribes-us-attorney>; <http://www.straitstimes.com/business/companies-markets/keppel-om-to-pay-us422m-in-fines-to-settle-bribery-probe>; <http://www.euronews.com/2017/12/26/keppel-bribery-fine-puts-spotlight-on-peer-sembcorp-shares-slide> accessed 1 December 2018.

1. Family-owned companies

Different studies have been conducted on the family-owned companies in Singapore. One study found that 69 out of the 100 largest companies are owned by families.[132] Another study found that 386 out of 743 companies (52%) listed on the Singapore Exchange (SGX) consist of family-owned companies, and the top 10 owners hold an average of 74% shares in family-owned companies.[133]

A more recent study found that 60.8% of the listed companies are owned by families.[134] And family firms constitute 33.1% of the market capitalisation.[135] The top 5 largest shareholders in family- owned companies own 69.5% of the shares, of which 38.3% are directly traceable to family members.[136] Notably, the top 20 largest shareholders in family-owned companies have 80.5% control of the voting rights.[137]

78.6% of CEOs and 72.9% of the chair of boards of directors are family members.[138] The CEO and chair are the same persons in 42.8% of family owned companies (whereas it is

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[132] Tan Lay Hong, *Exploring the Question of the Separation of Ownership from Control: An Empirical Study of the Structure of Corporate Ownership in Singapore's Top 100 Listed Companies* (Working paper) (2010) Appendix I.

[133] Marleen Dieleman and others, *Drawing a Portrait of Family Firm Governance in Singapore: A Study of SGX-Listed Family Firms* (Singapore: Centre for Governance, Institutions, and Organizations 2011) <https://bschool.nus.edu.sg/Portals/0/images/CGIO/Resources/CGIO-FBN%20Asia%20Family%20Business%20Presentation%2016%20Nov%202011.pdf> accessed 1 December 2018.

[134] Marleen Dieleman and others, *Success and Succession: A Study of SGX-listed Family Firms* (Singapore: Centre for Governance, Institutions, and Organizations, 2013) 2 <https://bschool.nus.edu.sg/Portals/0/images/CGIO/Report/Asian%20Family%20Business%20Report.pdf> accessed 1 December 2018.

[135] Ibid 10.

[136] Ibid 3.

[137] Ibid 24.

[138] Ibid 3.

17% in non-family companies).[139] The average length of directorship for founder-family-members is 20.7 years and 15.7 years for other family members, compared to 7.5 years for non-family member directors.[140] The numbers demonstrate that family members not only dominate the board and management, but they have also succeeded in entrenching themselves given the long tenure of their terms on the board and management. And in light of the fact that the board, which is dominated and entrenched by family members, has approved related party transactions (that are outside the scope of the listing rules and hence not subject to disinterested shareholder approval), extractions of private benefits of control are a strong possibility. For example, a survey of 69 family-owned companies found that related party transactions without shareholder approval (because they are not subject to listing rules) amount to S$960,374,117 and those with shareholder approval (because they are subject to listing rules), S$957,106,457.[141]

2. Government-linked companies

26 of the 100 largest companies are controlled by the Singapore government.[142] The Singapore government, through the Ministry of Finance (MOF), owns Temasek Holdings Pte Ltd which in turn controls 23 of Singapore's largest listed companies – the GLCs.[143] These 23

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[139] Ibid 17.

[140] Ibid 18.

[141] Tan Lay Hong, 'Family-Owned Firms in Singapore: Legal Strategies for Constraining Self-Dealing in Concentrated Ownership Structures' (2011) 23 *Singapore Academy of Law Journal* 890, 895.

[142] Tan Lay Hong, *Exploring the Question of the Separation of Ownership from Control: An Empirical Study of the Structure of Corporate Ownership in Singapore's Top 100 Listed Companies* (Working paper) (2010) 28 <http://docs.business.auckland.ac.nz/Doc/exploring-the-question-of-ownership-from-control.pdf> accessed 1 December 2018.

companies account for 37% of Singapore's total market capitalisation.[144] Studies have shown that the performance of GLCs are superior to non-GLC in terms of return on assets and equity[145] as well as corporate governance.[146] This is in stark contrast to the GLCs in Malaysia, the PSUs in India or the SOEs in Hong Kong.

There are two principal reasons for the success of the Singapore GLCs. First, the political legitimacy of the government depends on how well the GLCs have performed.[147] This is tied to the government's strategy to promote economic growth in Singapore through the GLCs since the founding of Singapore.[148] Second, the policy of Temasek is not to interfere in the business operations of the GLCs; rather, Temasek leaves the decision-making to the boards of the respective GLCs which are commercially run with a view to long-term profit maximisation.[149] This can be seen in the restrictions that are placed on (i) the MOF's control rights over Temasek and (ii) the acts of the board of Temasek.[150] On the former, under the Singapore constitution[151], the President of Singapore who does not sit on the board of Temasek,

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[143] Isabel Sim and others, *The State as Shareholder: The Case of Singapore* (Singapore: Centre for Governance, Institutions, and Organizations, 2014) 23–24 <https://bschool.nus.edu.sg/Portals/0/docs/FinalReport_SOE_1July2014.pdf> accessed 1 December 2018.

[144] Ibid 6.

[145]James S Ang and David K Ding, 'Government Ownership and the Performance of Government-Linked Companies: The Case of Singapore' (2006) 16 *Journal of Multinational Financial Management* 64, 85-86; Carlos D Ramirez and Ling Hui Tan, *Singapore, Inc. Versus the Private Sector: Are Government-Linked Companies Different?*, IMF Working Paper WP/o3/156 (2003) <https://www.imf.org/external/pubs/ft/wp/2003/wpo3156.pdf> accessed 1 December 2018.

[146] Isabel Sim and others, *The State as Shareholder: The Case of Singapore* (Singapore: Centre for Governance, Institutions, and Organizations, 2014) 6 <http://bschool.nus.edu/Portals/0/docs/FinalReport_SOE_1July2014.pdf> accessed 1 December 2018.

[147] Cheng-Han Tan and others, 'State-Owned Enterprises in Singapore: Historical Insights into a Potential Model for Reform' (2015) 28 *Columbia Journal of Asian Law* 61, 86-91.

[148] Ibid.

[149] Ibid.

[150] Dan W Puchniak and Luh Luh Lan, 'Independent Directors in Singapore: Puzzling Compliance Requiring Explanation' (2017) 65 *American Journal of Comparative Law* 265, 307-8.

[151] Constitution of the Republic of Singapore, Aug. 9, 1965, S 1/63, art. 22A.

and who cannot be affiliated with any political parties or engaged in any commercial activities, can veto the MOF's appointment or removal of the directors of Temasek.[152] Further, it is the board of Temasek and not its shareholder, MOF, who has the right to decide whether and if so how much dividends to be paid to MOF.[153]

Regarding the restrictions on the Temasek board, the board has to report to the president that every investment is transacted at fair market value[154], and the board has to obtain the permission of the president if it wishes to withdraw the reserves that Temasek has accumulated in the previous year.[155] Further, the Temasek Charter, which is a non-legally binding code of conduct, states that the board of Temasek does not interfere in the business or operations of the GLCs.[156] Finally, Temasek's finances are audited by an international firm and it discloses its financial information to the public.[157] That said, although there is no evidence of expropriation by Temasek, the controlling shareholder of the GLCs, it does not follow that there is no mismanagement or corruption in the GLCs.[158]

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[152] Isabel Sim and others, *The State as Shareholder: The Case of Singapore* (Singapore: Centre for Governance, Institutions, and Organizations, 2014) 16 <http://bschool.nus.edu/Portals/0/docs/FinalReport_SOE_1July2014.pdf> accessed 1 December 2018; FAQs: How is the President Involved with the Board of Temasek?, TEMASEK <http://www.temasek.com.sg/abouttemasek/faqs#> accessed 1 December 2018.

[153] Isabel Sim and others, *The State as Shareholder: The Case of Singapore* (Singapore: Centre for Governance, Institutions, and Organizations, 2014) 16.

[154] Ibid.

[155] Ibid; FAQs: How is the President Involved in the Protection of Temasek's Past Reserves?, TEMASEK <http://www.temasek.com.sg/abouttemasek/faqs#> accessed 1 December 2018.

[156] Temasek Charter <https://www.temasek.com.sg/en/who-we-are/our-purpose.html> accessed 1 December 2018.

[157] Isabel Sim and others, *The State as Shareholder: The Case of Singapore* (Singapore: Centre for Governance, Institutions, and Organizations, 2014) 16 <http://bschool.nus.edu/Portals/0/docs/FinalReport_SOE_1July2014.pdf> accessed 1 December 2018; FAQs: How is the President Involved with the Board of Temasek?, TEMASEK, 8, 16, 34 <http://www.temasek.com.sg/abouttemasek/faqs#> accessed 1 December 2018.

[158] (n 131).

III. Strategies for regulating extractions of private benefits of control are deficient

In this part (Part III), I provide the first justification as to why controlling shareholders in the listed companies in the four common law jurisdictions in Asia should be subject to fiduciary duties: the *ex ante* and *ex post* strategies for regulating extractions of private benefits of control by controlling shareholders are deficient.

There are two *ex ante* strategies that I will analyse, the first of which are the listing rules regulating related party transactions (RPTs) in the listed companies, and the second are participative mechanisms, namely, the rights of shareholders to attend and vote at the general meeting, as well as the right to requisition the company to convene general meetings.

Subsequently, I analyse four *ex post* strategies that could be used to control extractions of private benefits of control and I argue that they are problematic. The first is to subject controlling shareholders to the same duties as directors by using the doctrine of shadow directors, and the second is to use the doctrine of de facto directors. The third is to subject controlling shareholders to the same duty that is imposed on shareholders when they alter the articles (namely, to act bona fide for the benefit of the company as a whole). The fourth and final one is to use the mechanism of unfair prejudice/oppression to curb extractions of private benefits of control.

To be clear, the deficiencies in the existing legal strategies for regulating extractions of private benefits of control do not preclude reforms to these strategies. I do not argue that my proposed strategy of subjecting controlling shareholders to fiduciary duties should replace the existing deficient strategies. Nor do I argue that imposing fiduciary duties will solve all the problems with the existing laws. Rather, I argue that my proposed strategy will address some of the problems and will help to curb extractions of private benefits of control.

A. Ex ante: Rules on related party transactions (RPTs)

In this section, I put forward two major criticisms of the listing rules regulating RPTs. The first is that the mechanisms imposed by the listing rules for regulating RPTs – opinion/approval by the audit committee/independent directors' committee, as well as approval by the independent financial adviser and disinterested shareholders – are not effective in curbing extractions of private benefits of control by the controlling shareholders. Second, the listing rules do not regulate certain RPTs.

I discussed earlier that shareholders wield significant (albeit limited) powers under the laws of the four common law countries in Asia (Part I). And I showed that the majority of the listed companies in the four common law countries in Asia are dominated by controlling shareholders who are either families or the government. Where a company is dominated by a controlling shareholder, the latter wields substantial formal and informal power over the company. Moreover, the power of controlling shareholders is further entrenched when they either hold, or appoint their family members to, senior management positions in family-owned companies, the latter of which account for the majority of listed companies that have concentrated ownership structure in the four countries. With respect to the SOEs, the controlling shareholder which is the government normally entrenches its power by appointing its nominee directors to the board.

In light of the powers wielded by controlling shareholders, I have also explained in Part II that a major problem lies with their diversion of corporate wealth to themselves, by means of transfer of resources, at the expense of the company and minority shareholders. This is known as 'extractions of private benefits of control[159], a serious manifestation of which is 'tunnelling'.[160] A prime example of tunnelling involves the transfer of resources between controlling shareholders and the company through RPTs[161] which are essentially self-dealing transactions.[162] The resources consist of either cash or assets.[163] The difference between asset and cash flow tunneling is that the latter reduces the company's current cash flow but leaves the assets untouched. An example of cash flow tunneling is that the company buys goods or services from the controlling shareholders at above market price. Or the company sells goods and services to the controlling shareholder at below market price. Another example of cash flow tunneling is where a company makes a loan to the controlling shareholder at below market interest rate. A further example is executive compensation whereby the company pays the CEO who is the controlling shareholder at above market rate. Alternatively, the company could provide cash guarantees for the debts owed by the controlling shareholder or companies controlled by the latter. Asset tunneling refers to the transfer of tangible assets (such as property or equipment) or intangible assets (such as intellectual property or know-how) between the controlling shareholders and the company to the detriment of the company. For example, the

[159] Ronald J Gilson, 'Controlling Shareholders and Corporate Governance: Complicating the Comparative Taxonomy' (2006) 119 *Harvard Law Review* 1641, 1651; Ronald J Gilson and Alan Schwartz, 'Constraints on Private Benefits of Control: Ex Ante Control Mechanisms versus Ex Post Transaction Review' (2013) *Journal of Institutional and Theoretical Economics* 160, 161-2.

[160] Simon Johnson and others, 'Tunneling' (2000) 90 *American Economic Review* 22.

[161] Another type of tunnelling does not involve any transfer of resources but includes insider trading, squeeze-outs at below market value, share issues at below market value, and equity-linked compensation that is above market value. See Ronald J Gilson and Jeffrey N Gordon, 'Controlling Controlling Shareholders' (2003) 152 *University of Pennsylvania Law Review* 785.

[162] Simeon Djankov and others, 'The Law and Economics of Self-Dealing' (2008) 88 *Journal of Financial Economics* 430.

[163] Vladimir A Atanasov and others, 'Law and Tunnelling' (2011) 37 *Journal of Corporation Law* 1.

controlling shareholder can buy the assets from the company at below market rate or sell them at a preferential rate to the company.

RPTs are a pervasive method of tunneling and have attracted substantial literature in the Asian jurisdictions[164], and have been the subject of reforms in many jurisdictions.[165] Evidence of tunneling is reflected in many ways but with respect to RPTs, it is reflected in the decline in the value of the shares of the company after the announcement of RPTs.[166]

However, not all RPTs are value-decreasing. Some are value-enhancing. A handful of examples will suffice. A company wishes to sell its machinery. It is having difficulty finding suitable buyers. But the controlling shareholder is able and willing to do so. This saves the company considerable transaction cost. This is not only about cost-saving but about synergies and complementarities in light of the next example: the business of the listed company deals with the construction of luxury apartments. The controlling shareholder of the listed company is also the majority shareholder of another company that specialises in the sale and marketing of luxury apartments. The controlling shareholder is obviously knowledgeable about the business of the listed company and has invested significant resources in it. It would be appropriate for the company of which the controlling shareholder is a majority shareholder to enter into transactions with the listed company to market and sell those apartments.

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[164] See eg, Padmini Srinivasan, 'An Analysis of Related-Party Transactions in India' (September 30, 2013), IIM Bangalore Research Paper No. 402, 9-10 <https://ssrn.com/abstract=2352791> accessed 1 December 2018; Marianne Bertrand and others, 'Ferreting Out Tunneling: An Application to Indian Business Groups' (2002) 117 *Quarterly Journal of Economics* 121; Raja Kali and Jayati Sarkar, 'Diversification and Tunnelling: Evidence from Indian Business Groups' (2011) 39 *Journal of Comparative Economics* 349; Sarkar and Sarkar (n 15) 156-163; Cheung (n 19); Simon Johnson and Todd Mitton, 'Cronyism and Capital Controls: Evidence from Malaysia' (2003) 67 *Journal of Financial Economics* 351. In relation to Singapore, there is no clear evidence of tunnelling through RPTs but in one study, the authors used RPTs in the listed companies in Singapore as a proxy for tunnelling: see Agung Juliarto and others, 'Managerial Ownership Influencing Tunnelling Behaviour' (2013) 7 *Australasian Accounting Business & Finance Journal* 1, 12-13.

[165] Enriques (n 30) 8.

[166] See eg, Cheung (n 19).

Propping is another type of RPT but it is the opposite of tunneling as the controlling shareholder transfers resources from itself to the listed company usually but not exclusively when the company is experiencing liquidity or earnings difficulties.[167] There is evidence of propping in the listed companies in the four countries in Asia.[168] For example, a company has been suffering from negative return on equity, and there is a likely risk that it could be delisted under listing rules. The controlling shareholder decided to provide funding to the company, or it causes another subsidiary to provide preferential loan to the listed company. In short, propping includes but is not limited to the controlling shareholder transferring goods, services and assets to the listed company at below the market rate; the controlling shareholder providing cash, loan or loan guarantees to the listed company; and the controlling shareholder transferring funds from a financially healthy subsidiary to the listed company which is financially weaker.

However, there are at least three downsides to propping. First, it has been shown that controlling shareholders in the Asian jurisdictions would prop up companies by providing them with loans when the economy experiences moderate negative shock.[169] But when the moderate shock becomes more serious, controlling shareholders would stop propping and engage in tunnelling, thereby causing the company to collapse.[170] Second, there is research showing that after the controlling shareholders of listed Chinese SOEs propped up their companies because their motivation was to prevent the company from being delisted or deprived of the ability to issue new shares under the listing rules, the controlling shareholders then engaged in tunneling

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[167] Eric Friedman and others, 'Propping and Tunneling' (2003) 31 *Journal of Comparative Economics* 732. For a summary of the different definitions of 'propping', see Maggie P Williams and Dennis W Taylor, 'Corporate Propping Through Related-Party Transactions' (2013) 55 *International Journal of Law and Management* 28.

[168] Cheung (n 44); Sin Huei Ng and others, 'Profit Redistribution in Family-Controlled, Group-Affiliated Publicly-Listed Corporations in Malaysia' (2013) 10 *Corporate Ownership and Control* 142; Friedman, ibid.

[169] Friedman (n 167) 734, 748. The authors provided evidence that during the Asian financial crisis, the controlling shareholder provided loans to the company. But once the financial situation worsened, the controlling shareholder engaged in tunnelling. The reason is because of weak legal protection for creditors as they would not be able to enforce the collateral.

[170] Ibid.

to the detriment of those companies by causing the companies to lend money to the controllers at a preferential rate.[171] Finally, a study on Indian business groups found that controlling shareholders that provided loans from a stronger company to the financially weaker company within the group, thereby averting bankruptcy, are motivated by concerns that failure to prop up the weaker company would result in adverse financial information about the group being disclosed to external financiers and thus, it would be more difficult to extract private benefits of control because of more intense monitoring by external lenders.[172]

The purpose of the above analysis is to paint a nuanced picture of RPTs by showing that there are value-enhancing and value-decreasing RPTs. A key objective of the listing rules on RPTs, thus, ought to be the prevention of extractions of private benefits of control while allowing value-enhancing RPTs.[173] But I shall demonstrate below that it is doubtful that the RPT rules in the four common law systems in Asia can effectively curb extractions of private benefits of control. In other words, it is highly questionable that the existing rules can effectively minimise value-decreasing RPTs.[174]

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[171] Qianwei Ying and Liang Wang, 'Propping by Controlling Shareholders, Wealth Transfer and Firm Performance: Evidence from Chinese Listed Companies' (2013) 6 *China Journal of Accounting Research* 133; Guohua Jiang and Hansheng Wang, 'Should Earnings Thresholds Be Used As Delisting Criteria?' (2008) 27 *Journal of Accounting and Public Policy* 409.

[172] Radhakrishnan Gopalana and others, 'Affiliated Firms and Financial Support: Evidence from Indian Business Groups' (2007) 86 *Journal of Financial Economics* 759.

[173] OECD, *Guide on Fighting Abusive Related Party Transactions* (2009) <https://www.oecd.org/daf/ca/corporategovernanceprinciples/43626507.pdf> accessed 1 December 2018; Asian Corporate Governance Association, ACGA White Paper on Corporate Governance in India (2010) < https://www.acgaasia.org/upload/files/advocacy/20170402220450_115.pdf> accessed 1 December 2018; CFA Institute for Financial Market Integrity, Related Party Transactions: Cautionary Tales for Investors in Asia (2009) <https://www.cfapubs.org/doi/pdf/10.2469/ccb.v2009.n1.1> accessed 1 December 2018.

[174] Reforming the rules on RPT is one part of the story. Whether value-decreasing RPTs can be effectively curtailed also depends on contextual considerations such as cultural attitudes toward tunneling, as well as the quality of the rule of law, legal institutions and enforcement mechanisms: Enriques (n 30) 19-20.

In Hong Kong, Singapore and Malaysia, RPTs of a certain value[175] are regulated using three techniques: (i) a committee of independent directors, or an audit committee (comprising a majority of independent directors) has to issue an opinion[176]; (ii) an independent financial adviser has to issue an opinion;[177] and (iii) the RPT has to be approved by disinterested shareholders (which precludes the controlling shareholder and his associates from voting).[178] Moreover, the RPTs have to be publicly disclosed.[179] In India, RPTs of a certain value have to be approved by an audit committee[180] and the general meeting (via ordinary resolution)[181], and disclosure has to be made in the financial statements.[182]

But the main differences between India and the other three countries are that (a) the audit committee has to approve and not merely opine on the RPT[183]; (b) there appears to be no

[175] HKEX LR14A.76(2): equal to or more than 5% of assets or revenue; SGX LR 906: equal to or more than 5% of the group's latest audited net tangible assets; Bursa Malaysia LR 10.08(1) and 10.08(2): if the percentage ratios of a RPT is 0.25% or more, the listed issuer must account for the RPT to the Exchange. If the percentage ratio of the RPT is 5% or more, a listed issuer must send a circular to the shareholders, obtain shareholder approval in the general meeting and appoint an independent adviser.

[176] HKEX LR 14A 39 and LR 14A 40 (opinion of an independent committee is required, but note that the rules do not state how many independent directors are required, only that the committee must consists of independent non-executive directors who have no material interest in the transaction); SGX LR 917(4)(a)(ii), 920(b)(vi), 921(5) (opinion of the audit committee required if it takes a different view to the independent financial adviser) (see Provision 10.2 of the Code of Corporate Governance 2018 stating that the audit committee should consist of at least three members, the majority of whom should be independent and all members have to be non-executive); Bursa Malaysia LR Appendix 10C (3)(a) (the opinion of audit committee is required) (see LR 15.09(1)(b) stating that the audit committee must consist of at least three members, the majority of whom should be independent, and all members have to be non-executive).

[177] HKEX LR 14A 39, 14A 44 and 14A 45; Bursa Malaysia LR 10.08(2)(c) and 10.08(3); SGX LR 920(b)(v) and 921(4)(a).

[178] HKEX LR 14A 36; SGX LR 914 (an "interested person" must abstain from voting) and SGX LR 904(4)(a) (an "interested person" includes controlling shareholder of the issuer); Bursa Malaysia LR 10.08 (7)(a) and 7(b).

[179] HKEX LR 14A 35; SGX LR 905; Bursa Malaysia LR 10.08(1).

[180] Securities and Exchange Board of India (SEBI) Listing Obligations and Disclosure Requirements (LODR) 23(2) and 23(3) (opinion of audit committee) and 18(1)(b) (two-thirds of the audit committee should consist of independent directors).

[181] India Companies Act 2013 (IN CA), s 188(1).

[182] Accounting Standard (AS) 18 for Related Party Disclosures issued by the India Ministry of Corporate Administration.

[183] SEBI LODR 23(2) and 23(3).

need for any opinion from an independent financial adviser; and (c) the controlling shareholder is not prohibited from voting in the RPT as it does not appear to fall within the definition of related party[184] (unlike Hong Kong, Singapore and Malaysia where both the controlling shareholder and his associates must abstain).

	Singapore	Malaysia	Hong Kong	India
Committee of Independent Directors			X (opinion)	
Audit Committee	X (opinion)	X (opinion)		X (approval)
Independent Financial Adviser	X	X	X	
Disinterested Shareholders	X	X	X	

I will analyse the problems with each of the three mechanisms for approving RPTs, i.e. the independent directors' committee/audit committee, independent financial adviser, and disinterested shareholders. I will argue that these mechanisms do not effectively constrain extractions of private benefits of control by controlling shareholders.

To be clear, it is not my argument that subjecting controlling shareholders to fiduciary duties should replace the deficient rules on RPT. Nor is it my claim that imposing fiduciary duties can address all the problems arising from the rules on RPT. Rather, my claim is that it can supplement the rules on RPT and can help to address some of the problems. Moreover, nothing in my claim precludes reforms to the RPT rules. It is possible and desirable to reform

[184] IN CA, s 2(76). Cf Umakanth Varottil and Richa Naujoks, 'Corporate Governance' in Linda Spedding (ed) *India: The Business Opportunity* (Eastern Book Company 2016) 321-322 (arguing that 'any related party shareholder interested in the transaction is disallowed from voting. This introduces the concept of a "majority of the minority" voting…'). But under IN CA, s 2(76), the definition of 'related party' does not include the controlling shareholder in question.

the RPT rules and impose fiduciary duties. Even if the RPT rules are successfully reformed to effectively minimise tunnelling by controlling shareholders, there are other types of conflicts of interest involving controlling shareholders that are not related to RPTs but which can give rise to extractions of private benefits of control (discussed in Part IV below), and in this context, it would still be advisable to impose fiduciary duties on controlling shareholders. In other words, reforming the RPT rules is a limited and piecemeal solution that does not address a deeper and widespread problem concerning conflicts of interest between the controlling shareholders and the company in other contexts. Further, in view of the fact that controlling shareholders wield significant formal and informal discretionary powers over the company (in the form of voting rights and influence) and they can exercise these powers to the detriment of the company (discussed earlier in Parts I and II), imposing fiduciary duties would be appropriate. Subjecting controllers to fiduciary duties, it is suggested, is a more coherent solution.[185]

1. Independent directors'/audit committee opinion or approval

To begin with, approval is not required from the independent directors' committee or audit committee in Singapore, Malaysia and Hong Kong; only an opinion as to whether to recommend or reject the RPT. However, in India, approval from the audit committee is required.

[185] An analogy can be drawn with directors. It would be insufficient and inappropriate if fiduciary duties are imposed on directors only with respect to self-dealing transactions, which would be the equivalent of RPTs involving controlling shareholders. There are other types of conflicts of interest between directors and the company that do not relate to self-dealing transactions. Further, similar to controlling shareholders, directors wield significant and substantial discretionary powers over the company and they can exercise them to the company's detriment.

In Hong Kong, the committee of independent directors, after taking into account the opinion of the independent financial adviser, must advise the disinterested shareholders on matters including whether the terms of the connected transaction are fair and reasonable; whether the connected transaction is in the interests of the listed issuer and its shareholders as a whole; and how to vote on the connected transaction.[186] In Malaysia, the audit committee has to provide its opinion as to whether the transaction is on normal commercial terms, and whether it is prejudicial to the interests of the issuer and its minority shareholders.[187] Thus, in Hong Kong and Malaysia, although advice/opinion is required from the independent directors' committee or audit committee, it is not binding. In Singapore, it is remarkable that the audit committee does not even need to provide an opinion unless it takes a different view from the independent financial adviser.[188] Even so, the opinion is not binding. Although the opinion of the independent directors'/audit committee in Hong Kong, Singapore and Malaysia is not binding, the opinion still serves an important function and therefore we should critically analyse the independence of the directors who give the opinion. This is because the opinion has to be publicly disclosed before the disinterested shareholders can make the decision. Given that disinterested shareholders will usually not have the expertise or information-gathering power to understand the purpose and nature of the RPT, they will rely on what the committee and independent financial adviser opines. In India, however, approval from the audit committee (of which there must be at least three directors, of whom two must be independent[189]) is required.[190]

[186] HKEX LR 14A.40.

[187] Bursa Malaysia, Appendix 10D, Main LR 6.

[188] SGX LR 921(5).

[189] IN CA, s 177(2).

[190] SEBI LODR 23(3)(c).

However, the mechanism of the audit committee (used in Singapore, Malaysia and India) and the independent directors' committee (used in Hong Kong) is unlikely to effectively control tunneling by controlling shareholders because of four problems.[191] First, the independent directors can be removed by the controlling shareholders. Second, the independent directors are appointed by the general meeting and nominated by the nominating committee, both of which are under the control of the controlling shareholder. Third, controlling shareholders exercise significant control over the directors in family-owned companies and SOEs. Fourth and finally, under the rules, the independent directors are not necessarily independent. I elaborate on each of these criticisms below.

i) Independent directors can be removed by controlling shareholders

First, although independent directors will certainly have more expertise than disinterested shareholders to critically evaluate the merits of RPTs, directors, including independent directors, in a listed company can be removed anytime without cause by ordinary resolution even if it is contrary to the company's constitution.[192] Given that the majority of the

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[191] For a detailed analysis of independent directors and their effect on corporate governance in Hong Kong, Singapore and India, see Dan W Puchniak and others (eds), *Independent Directors in Asia: A Historical, Contextual and Comparative Approach* (CUP 2017). The literature shows that there is no correlation between independent directors and corporate governance or corporate performance in India, Malaysia and Hong Kong: see eg AK Garg, 'Influence of Board Size and Independence on Firm Performance: A Study of Indian Companies' (2007) 32 *VIKALPA* 39; Haslindar Ibrahim and Fazilah Abdul Samad, 'Corporate Governance Mechanisms and Performance of Public Listed Family-Ownership in Malaysia' (2011) *3 International Journal of Economics and Finance* 105; Sidney Leung and others, 'Corporate Board and Board Committee Independence, Firm Performance, and Family Ownership Concentration: An Analysis Based on Hong Kong Firms' (2014) 10 *Journal of Contemporary Accounting and Economics* 16. Regarding Singapore, it has been argued that, functionally, independent directors have been effective in signalling good corporate governance, but there is no convincing empirical evidence that having independent directors has actually resulted in an increase in share price: Dan Puchniak and Luh Luh Lan, 'Independent Directors in Singapore: Puzzling Compliance Requiring Explanation' (2017) 65 *American Journal of Comparative Law* 265. For a trenchant critique from a Western perspective, see eg, Wolf-Georg Ringe, 'Independent Directors: After the Crisis' (2013) 14 *European Business Organization Law Review* 401.

[192] Hong Kong Companies Ordinance ('HK CO') (Cap 622), s 462; Singapore Companies Act ('SG CA') (Cap 50), s 152; Malaysian Companies Act 2016 ('MY CA'), s 206(2); IN CA s 169. Although directors can be removed by ordinary resolution in India, the Indian Companies Act does not contain the language that appears in the

listed companies in the four countries in Asia are dominated by controlling shareholders who control the general meeting, independent directors can be easily dismissed, particularly those who defy the wishes of the controlling shareholders. Thus, the power wielded by controllers over independent directors is likely to colour their assessment of whether to approve or reject the RPTs; this increases the risk that RPTs from which controlling shareholders can extract private benefits of control will not be rejected.[193]

ii) The general meeting and nominating committee are under the control of the controlling shareholder

Second, independent directors are appointed by the general meeting[194], which is usually under the control of the controlling shareholders, and the independent directors are nominated by a nominating committee[195] (or in India, selected from a data bank[196]). And the nominating committee is composed of a majority of independent directors[197], who are themselves appointed by the controlling shareholders who could in turn dismiss them. Thus, controlling shareholders may exert considerable influence on the nominating committee. In addition to

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companies legislations of the other three jurisdictions which states that directors can be removed notwithstanding anything in the company's constitution or in any agreement between the company and him.

193 Lucian A Bebchuk and Assaf Hamdani, 'Independent Directors and Controlling Shareholders' (2016) 165 *University of Pennsylvania Law Review* 1271, 1286-1287.

194 Hong Kong Model Articles, art 22; HK CO, s 460(2); SG CA, s 149B; MY CA, s 203(1); IN CA, s 150(2).

195 In Hong Kong, see HKEX LR, A5.2b and 5.5 of Appendix 14. In Singapore, see Singapore Code of Corporate Governance 2018, Provision 4.1(d). In Malaysia, see Bursa Malaysia LR 15.08A. In India, see IN CA, s 178(2).

196 See IN CA, s 150: '…an independent director may be selected from a data bank containing names, addresses and qualifications of persons who are eligible and willing to act as independent directors, maintained by any body, institute or association, as may by notified by the Central Government, having expertise in creation and maintenance of such data bank and put on their website for the use by the company making the appointment of such directors.'

197 In Hong Kong, see HKEX LR, A5.2b of Appendix 14. In Singapore, see the Code of Corporate Governance 2018, Provision 4.2. In Malaysia, see Bursa Malaysia LR 15.08A.

appointment and dismissal, the re-appointment of independent directors also requires the approval of the general meeting.[198] It would be unlikely for independent directors who wish to be re-elected to act against the wishes of the controlling shareholders.[199] Further, independent directors who have been serving for a long period of time would arguably have a greater desire to be re-elected and hence even more reluctant to defy the controlling shareholders. This is because it would be more difficult for them to find new jobs in view of their age[200], which makes it more difficult for them to adjust to new business challenges.[201]

iii) Controlling shareholders exercise significant influence in family-owned companies and state-owned enterprises

The third problem is linked to, but distinct from, the second. Controlling shareholders exercise significant formal and informal powers over the board of directors in family-owned companies and SOEs. Family-owned companies account for the majority of the listed companies in Asia.[202] There is evidence that controlling shareholders exert control over these

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[198] See Malaysian Code on Corporate Governance 2017, 23: After an independent director has served on the board for 9 years and wishes to be retained, he must seek annual shareholders' approval. In India, see IN CA, ss 149(10) and (11): An independent director is eligible for re-appointment after serving a term of 5 years on the passing of a special resolution by the company and disclosure of such appointment in the board's report. Yet, an independent director can at most serve only 2 terms, a maximum of 10 years. In Hong Kong, see the Code of Corporate Governance, A.4.3: 'If the independent director has served for a term of 9 years, any further appointment of such independent non-executive director should be subject to a separate resolution to be approved by shareholders.' The board should set out to shareholders in the papers accompanying a resolution to elect such an independent non-executive director the reasons they believe that the individual continues to be independent and why he should be re-elected. In Singapore, see Code of Corporate Governance 2018, footnote 5 to Provision 2.4: a director who has been a director for more than 9 years and whose continued appointment as an independent director has not been sought and approved in the special procedures described therein is not considered an independent director.

[199] Yaron Nili, 'The "New Insiders": Rethinking Independent Directors' Tenure' (2016) 68 *Hastings Law Journal* 97, 122.

[200] Nikos Vafeas, 'Length of Board Tenure and Outside Director Independence' (2003) 30 *Journal of Business Finance & Accounting* 1043, 1045.

[201] Judy Canavan and others, 'Board Tenure: How Long is Too Long?' (2004) 28 *Boards & Directors* 39, 40.

[202] See the percentage of family controlled firms in CFA Institute, *Corporate Governance for Asian Publicly Listed Family-Controlled Firms* <http://www.cfapubs.org/doi/pdf/10.2469/ccb.v2017.n1.1> accessed 1

companies by appointing themselves or their associates to the board of directors,[203] and these executive directors in turn exercise influence over the independent directors in two ways.

First, the board of directors delegates power, and is responsible for providing resources, to the nominating committee so that the latter can discharge its responsibilities, which include conducting assessments as to the independence of the proposed director for consideration by the general meeting. Second, it is possible for the controlling shareholder, who is a director, to appoint himself to the nominating committee because the listing rules in the four countries only requires a majority of the nominating committee to comprise independent non-executive directors. Connected to this point is that, crucially, the controlling shareholder who is a director can also be a member of the audit committee as the rules in the four countries in Asia only require a majority of the audit committee to consist of independent directors.[204] But even if the controlling shareholder or his associate is not a director, the controller can still exert influence on the board (given that he has the power to appoint and dismiss the board), who can in turn exert influence on the nominating committee by restricting its authority and resources. Finally, because independent directors in family owned-companies are generally perceived by the controlling shareholders as threats to their authority because of their interference with the

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December 2018. In Hong Kong, 62% of all publicly listed firms are family firms. In Singapore, it is 63%. In Malaysia, it is 62%. In India, it is 67%.

[203] CFA Institute, *Corporate Governance for Asian Publicly Listed Family-Controlled Firms* 3 <http://www.cfapubs.org/doi/pdf/10.2469/ccb.v2017.n1.1> accessed 1 December 2018; Stijn Claessens and others, 'Disentangling the Incentive and Entrenchment Effects of Large Shareholdings' (2002) 57 *Journal of Finance* 2741; Joseph PH Fan and others, 'Corporate Finance and Governance in Emerging Markets: A Selective Review and an Agenda for Future Research' (2011) 17 *Journal of Corporate Finance* 207, 212. Note that under the listing rules of the four countries in Asia, the board of directors of the listed company must consist of a minimum number of independent non-executive directors. HKEX LR3.10: Hong Kong requires at least three independent non-executive directors; 2018 Singapore Code of Corporate Governance, footnote 7 to Provision 2.2: with effect from 1 January 2022, Rule 210(5)(c) of the SGX Listing Rules requires independent directors to make up at least one-third of the Board. Prior to that, Principle 2.1 of 2012 Singapore Code of Corporate Governance which states that independent directors should make up at least one-third of the Board, applies; Bursa Malaysia LR 15.02(1): A listed issuer must ensure that at least 2 directors or 1/3 of the board of a listed issuer, whichever is higher, are independent directors; IN CA, s 149(4): the board should consist of 1/3 independent directors.

[204] In all the four countries, the audit committee must consist of at least three directors, of whom a majority must consist of independent directors: HKEX LR 3.21; Singapore Code of Corporate Governance 2018, Provision 10.2; Bursa Malaysia LR 15.09(1)(b); SEBI LODR 18(1)(b).

decision-making process[205], it is likely that controlling shareholders will seek to either limit the power or influence the decisions of the independent directors.

In sum, controlling shareholders exercise control over independent directors through two mechanisms, namely, the general meeting and the board of directors (through the nominating committee). As a result, there is a risk that any assessment made by the audit committee or independent directors' committee as to whether or not the RPT should be approved will be skewed in favour of the controlling shareholder. It would be difficult for the audit committee to recommend rejecting RPTs that are favoured by the controlling shareholders. This increases the risk of extraction of private benefits of control.

In relation to the SOEs, the government as the controlling shareholder also exerts significant power over the directors (including independent directors) in the three jurisdictions (possibly with the exception of Singapore[206]). Regarding the GLCs in Malaysia, it has been said that the government used the GLCs to promote its own agenda and the board and management are expected to do its bidding.[207] This suggests that it is unlikely that the audit committee will reject value-decreasing RPTs. In relation to the PRC SOEs listed in Hong Kong, the listing rules stipulate that PRC governmental bodies are not normally subject to the rules regulating RPTs.[208] Thus, RPTs entered into between the PRC government and the company may require only board approval. Given that the PRC government appoints the board[209], and

[205] Sidney Leung and others, 'Corporate Board and Board Committee Independence, Firm Performance, and Family Ownership Concentration: An Analysis Based on Hong Kong Firms' (2014) 10 *Journal of Contemporary Accounting and Economics* 16, 17.

[206] As discussed in Part II, the controlling shareholder of the Singapore GLCs, Temasek, does not interfere with the decision-making process of the boards of the GLCs. That said, Temasek does have leverage over the directors of the GLCs as the power of dismissal and appointment lies with it.

[207] See Part II of Chapter 3.

[208] HKEX LR 14A.10. But note that '[t]he Exchange may request a listed issuer to explain its relationship with a PRC Governmental Body and why it should not be treated as a connected person.'

[209] See Part II of Chapter 3.

as the directors and management are beholden to the government and depend on the latter for career advancement and other benefits[210], the board is unlikely to reject value-decreasing RPTs. In India, given that transactions between two government companies are exempted from the listing rules[211], only board approval is required. And because the government not only exercises significant power over the nomination and appointment of directors[212] but also makes the strategic decisions for the company[213], value-decreasing RPTs are unlikely to be rejected.

iv) Independent directors are not necessarily independent from the controlling shareholders

Fourth and finally, the independent directors are not necessarily independent from the controlling shareholders. As a result, they are less likely to oppose value-decreasing RPTs. The four countries provide useful examples.

In Hong Kong, for example, a director is not precluded from being qualified as an independent director even if he is connected with a 10% shareholder, director or CEO of the listed company.[214] This is because it is only one of the eight factors that are used to assess the independence of a director.[215] The rule states that 'none of [these eight factors] is necessarily

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210 Ibid.

211 SEBI LODR 23(5)(a).

212 See Part II of Chapter 3.

213 Ibid.

214 HKEX LR 3.13(6): 'Connected' is defined in terms of immediate family members (including wife, husband, parent, child, step-child, brother, step-brother, sister, and step-sister) but excluding extended family members (such as aunties, uncles, nephews and nieces).

215 HKEX LR 3.13. The other seven factors are that the person (1) holds more than 1% of the number of issued shares of the listed issuer; (2) has received an interest in any securities of the listed issuer as a gift, or by means of other financial assistance, from a core connected person (i.e. 10% shareholder, director or CEO) or the listed issuer itself; (3) is a director, partner, principal or employee of a professional adviser who provides or (one year before the appointment) provided services to the listed issuer; (4) has a material interest in any principal business activity of or is involved in any material business dealings with a core connected person, listed issuer, its

conclusive.'[216] And '[i]ndependence is more likely to be questioned' if these factors are not complied with.[217] This implies that a director will not be disqualified from being an independent director even if he is connected with a 10% shareholder, provided that he has complied with all of the remaining seven factors or some of them. An important element in the assessment of independence under the Hong Kong listing rules is that considerable discretion is given to the independent director to evaluate and weigh the eight factors for the purpose of submitting to the listing authority a written confirmation as to whether he is independent in relation to each of the eight factors.[218] In practice, it is the nominating committee, on whom the controlling shareholders is likely to exert influence, that will prepare a report explaining whether the candidate is an independent director for consideration by the general meeting. And the general meeting, comprising the controlling shareholder, has the sole power of appointment and dismissal.

In Singapore, the definition of independence is under-inclusive and ambiguous. The 2018 Code of Corporate Governance defines an 'independent' director as 'one who has no relationship with the company, its related corporations, its 5% (and above) shareholders or its officers that could interfere, or be reasonably perceived to interfere, with the exercise of the director's independent business judgement in the best interests of the company.'[219] The Code[220] refers to the listing rules[221] (which took effect from January 2019) which state that a director

subsidiaries or parent company; (5) is on the board specifically to protect the interests of an entity whose interests are not the same as those of the shareholders as a whole; (6) is, or two years before the date of his appointment been, an executive or director (other than an independent non-executive director) of core connected person, listed issuer, its holding company, subsidiaries; and (7) is financially dependent on any of the core connected person, listed issuer, its holding company or subsidiaries.

[216] Ibid.

[217] Ibid.

[218] HKEX LR 3.13.

[219] Singapore Code of Corporate Governance 2018, Provision 2.1.

[220] Ibid, footnote 6.

is not independent if (i) he is employed by the company currently or was employed in the past three years; or (ii) he has an immediate family member who is or in the past three years has been employed by the company and whose remuneration is determined by the remuneration committee. The definition is under-inclusive as it implies that a director will still be regarded as independent even if his relatives or business associates are directors of the company. He will also still be regarded as independent even if his immediate family members hold senior management positions in the company as long as their remuneration is not determined by the remuneration committee.

Further, the meaning of the term 'no relationship' in the definition of independence is highly ambiguous. It is unclear if a director is independent even if he provides goods and services to the controlling shareholder, is financially dependent on the controlling shareholder, receives from the controlling shareholder gifts comprising shares of the listed company, or works or used to work for the controlling shareholder. To give a concrete example of the latter: it has been shown that half of the 148 directors of the GLCs that are classified as independent currently hold or have held positions in the government,[222] out of which 40% currently hold and 30% previously held positions with the Ministry of Finance, which is the ultimate controlling shareholder of the Singapore GLCs.[223] The figures suggest that even if the government does not direct or instruct the independent directors, the independent directors are not likely to defy the wishes of the controller, particularly those who presently hold positions in the ultimate controlling shareholder, i.e. Ministry of Finance.[224] It is unclear if these independent directors would still qualify as independent.

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[221] SGX LR 210(5)(d)(i) and (ii).

[222] Dan Puchniak and Luh Luh Lan, "Independent Directors in Singapore: Puzzling Compliance Requiring Explanation" (2017) 65 *American Journal of Comparative Law* 265, 313.

[223] Ibid 315.

[224] Kyle J Hatton and Katharina Pistor, 'Maximizing Autonomy in the Shadow of Great Powers: The Political Economy of Sovereign Wealth Funds' (2012) *50 Columbia Journal of Transnational Law* 47. But Puchniak and

In India, Clause 49 of the Listing Agreement defines an independent director as 'a non-executive director, other than a nominee director of the Company who fulfills the criteria of independence as laid down in the Listing Agreement which is similar to the Companies Act.'[225] The listing rules set out seven factors for assessing the independence of directors.[226] Section 149(6) of the Companies Act 2013 prescribes six criteria for assessing the independence of the independent director. It is unclear whether all six criteria must be satisfied or whether it suffices if one or more of the criteria are satisfied. The wording of the section indicates that it is not necessary for all six criteria to be satisfied because s 149(6) states: 'An independent director in relation to a company, means a director other than a managing director or a whole-time director or a nominee director — (a) who, in the opinion of the Board, is a person of integrity and possesses relevant expertise and experience; (b)…. (c)…. (d)… (e)…. *or (*f) who possesses such other qualifications as may be prescribed.' The word 'or' suggests that the six criteria can be read disjunctively rather than conjunctively. Section 149(7) states that the independent director must 'give a declaration that he meets the criteria of independence as provided in sub-section (6).' Again, it is not clear whether he can still be considered independent if he satisfies, say two, but flouts, say four, of the criteria.[227] Even if the director only complies with a minority of the criteria, it seems that the general meeting is not barred from appointing that person as the independent director. After all, what is required is merely an explanatory statement annexed

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Lan (at 315) are of the view that interference is unlikely because (a) the other 50% do not hold government positions; (b) 59.81% of the current positions and 70.73% of the past positions were in government bodies other than the Ministry of Finance and (c) Singapore is generally known for its transparency and meritocracy.

[225] SEBI LODR16(1)(b).

[226] Ibid.

[227] For example, it is not clear if a director will still be considered an independent director if he is not "related to" (a term which is not defined) the controlling shareholder and has no pecuniary relationship with the controlling shareholder but he used to be the chief technology officer of the listed company one year before he was appointed as an independent director or his relative has engaged in transactions with the company that is more than 2% of the annual gross turnover.

to the notice of the meeting stating the reasons for selecting the appointee as an independent director.[228]

Perhaps more importantly, in 2017, the Chairman of the Securities and Exchange Board of India (SEBI) complained about the lack of independence of the independent directors. He said that the independent directors are appointed at the mercy of the controlling shareholders and that many of the independent directors do not have the requisite qualifications. [229] He further noted that friends of the controlling shareholders are being appointed as independent directors simply for the sake of meeting the requirements of the Companies Act and listing rules. [230]

Other evidence of the significant influence that controlling shareholders wield over independent directors is that in the PSUs in India, the board members, including the independent directors, are nominated and appointed by the government who is the controlling shareholder.[231] The board has little control over the nomination of the independent directors. And tellingly, many of these independent directors in the PSUs used to work in the government and have political ties.[232] Thus, not only is it unlikely that the independent directors would monitor the government who is the controlling shareholder, but it is also unlikely that they will defy the wishes of the government. This suggests that they are less likely to reject value-decreasing RPTs.

In Malaysia, the first problem concerns the definition of independence. The listing rules define independence as '… a director who is independent of management and free from any

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[228] IN CA, s 150(2).

[229] 'Independent Directors Aren't Really "Independent", Says Sebi Chief' *National Herald* (29 June 2017).

[230] Ibid.

[231] S Subramanian, 'A Comparison of Corporate Governance Practices in State-Owned Enterprises and Their Private Sector Peers in India' (2016) 5 *IIM Kozhikode Society & Management Review* 200, 204.

[232] Ibid 208.

business or other relationship which could interfere with the exercise of independent judgement or the ability to act in the best interests of an applicant or a listed issuer.'[233] The rules then specify seven non-exclusive factors for determining the independence of the director. Similar to the problem in Hong Kong and India, it is not clear whether all these factors have to be complied with or whether it is sufficient if some or most of the factors have been complied with. For example, it is not clear whether a director would still be considered independent if he complies with all the seven factors save for two: he is a family member of the controlling shareholder and has engaged in transactions with the listed company. As a result, significant discretion is given to the board through its nominating committee, on whom the controlling shareholders exercise influence, to assess and select who they regard as independent. The recommendations of the nominating committee are then passed on to the general meeting to approve (or reject) the nominees. The second problem is that the independent directors do not actively monitor the management or play an active or effective role in corporate governance. In family-owned companies, the controlling shareholders prefer to keep control to themselves and their family members and to minimise the involvement of independent directors.[234] In GLCs, there is research suggesting that independent directors have negligible impact on the financial performance of the company.[235] Thus, in view of these two problems where firstly, the independent directors may be subject to the influence of controlling shareholders or may

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[233] Bursa Malaysia LR 1.01.

[234] Saeed Pahlevan Sharif and others, 'The Acquisition of Valuable Resources by Family-Controlled Companies in Malaysia Through Political Connections of Their Independent Directors' (2015) 49 *Journal of Developing Areas* 309; Noor Afza Amran and Ayoib Che Ahmad, 'Board Mechanisms and Malaysian Family Companies' Performance' (2011) 2 *Asian Journal of Accounting and Governance* 15, 18; Chin Fei Goh and Amran Rasli, 'CEO Duality, Board Independence, Corporate Governance and Firm Performance in Family Firms: Evidence from the Manufacturing Industry in Malaysia' (2014) 13 *Asian Business & Management* 333, 337-338; Chee Yoong Liew and others, 'Family Firms, Expropriation and Firm Value: Evidence of the Role of Independent Directors' Tenure in Malaysia' (2017) 6 *International Journal of Organizational Leadership* 42.

[235] Mansor Isa and Siew-Peng Lee, 'The Performance of Government-Linked Companies in Malaysia' (2016) 24 *Capital Markets Review* 1; Chee Wooi Hooy and Chwee Ming Tee, 'Directors' Pay Performance: A Study on Malaysian Government Linked Companies' Centre for Policy Research and International Studies, USM, 2009, 13-14.

not be independent from the controlling shareholders, and secondly, may not be willing or able to play an active or effective role in monitoring the controlling shareholders and management, independent directors are less likely to reject value-decreasing RPTs.

The above problems illustrate an important point: the actual or potential, direct or indirect, subtle or overt, interference by controlling shareholders in the nomination, appointment, dismissal and reappointment of independent directors.[236] This calls into question whether the mechanism of the independent directors' committee/audit committee can effectively curb extractions of private benefits of control in RPTs.

2. Independent financial adviser opinion

It may be argued that even if the independent directors are not independent or ineffective, the listing rules in Hong Kong, Singapore and Malaysia impose an additional layer of protection: an independent financial adviser must be appointed to issue an opinion regarding the RPT.

However, there are two key problems. First, the independent financial adviser might not be independent as there could be a conflict of interest because the independent financial adviser used to advise, or is currently advising, the company or controlling shareholder in a different transaction. Even if that is not the case, they might wish to be engaged by the company

[236] Given the problems with independent directors in the four Asian countries, an intriguing issue is what the rationales for having and maintaining the regime of independent directors are. Several reasons have been given. A political explanation is that having independent directors acts as a signal to the rest of the world that these countries have reputable corporate governance standards and yet the interests and powers of the key stakeholders, i.e. the controlling shareholders, are not threatened because the appointment and removal power lies exclusively with them, which power is subject to no legal constraints.

or the controlling shareholder in future transactions and as such may be reluctant to antagonise the controlling shareholder.[237] For example, in Hong Kong, although an independent financial adviser who has a current business relationship with the listed company or the controlling shareholder will not be considered independent, it will still be regarded as independent if 'the relationship arises under the independent financial adviser's appointment to provide the advice.'[238] This effectively creates an exception for those transactions (not related to the RPT in question) in which the listed company has engaged the independent financial adviser to provide advice. For example, the company has engaged KPMG to provide advice on restructuring and compliance with anti-money laundering regulations. Under the listing rules, the company can also engage KPMG as an independent financial adviser with respect to RPTs. Given that KPMG wants continuous business as an independent financial adviser from the listed company, and because it wants to maintain its other business relationships with the listed company or controller, KPMG is not likely to recommend rejection of the RPT. In Malaysia, the practice guide, which is not binding, states that the independent adviser has to confirm that there is no actual or potential conflict of interest and has to disclose the nature of any professional relationships in the past two years.[239] But the guide does not specify what amounts to a conflict of interest. In Singapore, the listing rules merely state that the independent financial adviser has to be 'acceptable to the Exchange' but no guidelines or criteria appear to have been stipulated as to what is meant by that phrase. Thus, significant discretion is given to the listing authority and much depends on the Exchange's willingness and ability to closely monitor those appointments.

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[237] See eg, Steven M Davidoff, 'Fairness Opinions' (2006) 55 *American University Law Review* 1557, 1586-1588.

[238] HKEX GEM LR17.96(4).

[239] Section 2.3, Best Practice Guide in Relation to Independent Advice Letters, <http://www.bursamalaysia.com/misc/system/assets/10737/listing_requirement_guidelines_independent_advice_letters.pdf> accessed 1 December 2018.

Second, the contents of the opinion of the independent financial adviser differ: they range from highly detailed and rigorous to cursory and superficial. In Hong Kong, the opinion must state: the justifications for making the opinion, the key assumptions made, the factors taken into consideration, and whether the terms of the RPT are fair and reasonable, whether the RPT is in the interests of the company and shareholders as a whole, whether the RPT is on normal commercial terms or better and whether in the ordinary course of business, and whether shareholders should vote in favour of the RPT.[240] Malaysia is similar to Hong Kong.[241] By contrast, in Singapore, the independent financial adviser only has to state in its opinion whether the transaction (i) is on normal commercial terms, and (ii) is prejudicial to the interests of the issuer and its minority shareholders.[242] Tellingly, in a study of the opinions of the independent financial adviser given in the context of RPTs and takeovers in Singapore, it was found that the opinions do not state whether the terms of the RPT are fair and reasonable but instead used tests that are more equivocal and hence less helpful; the rules give significant discretion to independent financial advisers as to the choice of methodologies and assumptions which can be skewed in favour of the RPTs; and it is very difficult for investors to sue the company or independent financial adviser should the latter have been negligent in issuing the opinions.[243] Thus, in view of the two problems above, the independent financial adviser mechanism still cannot address the problem of lack of independence of the independent directors.

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[240] HKEX LR14A.45.

[241] Bursa Malaysia LR, Appendix 10D, para 5.

[242] SGX LR 921(4)(a).

[243] Wai Yee Wan, 'Independent Financial Advisers' Opinions for Public Takeovers and Related Party Transactions in Singapore' (2012) 30 *Corporate and Securities Law Journal* 32, 33.

3. Disinterested shareholders' approval

The requirement for disinterested shareholders' approval only applies to Singapore, Hong Kong and Malaysia but not to India. India requires approval from the audit committee and the general meeting but the problem is that the controlling shareholder is not precluded from voting in the general meeting. Moreover, given that the controlling shareholder controls the appointment and dismissal of the directors in the audit committee, and the controller himself can be a member of the audit committee, it is very likely that the RPTs in India will be approved by the audit committee and the general meeting. This is hardly an effective *ex ante* mechanism to prevent extractions of private benefits of control.

In Singapore, Hong Kong and Malaysia, there are two key problems with the disinterested shareholders' approval mechanism. First, the disinterested shareholders may not be disinterested. The RPT rules in Hong Kong[244], Singapore[245] and Malaysia[246] prohibit 'associates'[247] or 'persons connected to'[248] the controlling shareholder from voting. The term 'associate' or 'person connected to' is defined to include immediate family members but not relatives (i.e. uncles, aunties, cousins and nephews) and friends of the controlling shareholder. Thus, the relatives and friends of the controlling shareholder are more likely than not to vote in favour of the RPT, by siding with the controlling shareholders. Second, in deciding whether

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[244] HKEX LR 14A.36; LR 2.16.

[245] SGX LR 919.

[246] Bursa Malaysia LR 10.08(7).

[247] HKEX LR 14A.12-14A.15; SGX LR Definitions and Interpretations.

[248] Bursa Malaysia LR 1.01.

to vote for or against the RPT, the minority shareholders will rely on the opinions of the independent directors' committee/audit committee and independent financial adviser, instead of expending additional resources at their own expense to conduct a separate investigation of the RPT on their own. After all, they face free rider and collective action problem, and studies have shown that they are generally passive.[249] However, the use of the independent directors' committee/audit committee and independent financial adviser has been shown to be highly problematic.

4. RPTs that are not subject to the listing rules

There are three types of RPTs that are exempted from the listing rules (i.e. they are not regulated by the mechanisms of audit committee, independent financial adviser and disinterested shareholders). Thus, only the board of directors, the power of appointment and dismissal of which lies solely in the hands of controlling shareholders, has to approve the transaction.

[249] In relation to US institutional shareholders, see eg, Lucian A Bebchuk and others, 'The Agency Problems of Institutional Investors' 31 (2017) *Journal of Economic Perspectives* 89; and Dorothy Lund, "The Case Against Passive Shareholder Voting (2018) 43 *Journal of Corporation Law* 493. Indian institutional shareholders are generally passive: see eg, Umakanth Varottil, 'The Advent of Shareholder Activism in India' (2012) 6 *Journal on Governance* 582, 593; Sunita Upenda Sharma, 'A Study of Small Shareholders' Attitude Towards Small-Shareholder Activism' (2016) 9 *Indian Journal of Corporate Governance* 67. There is no evidence disproving that institutional and retail shareholders are generally passive in Singapore and Hong Kong. There is evidence of hedge fund activism in Hong Kong but the activism is not targeted at RPTs but takes place in the context of share buy-backs, special dividends and going private transactions: see Frank Wong, "Shareholder Engagement and Activism Under the Radar: Empirical Evidence From Hong Kong (2003-15) — Rethinking Disclosure of Interests Regime" <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2725318> accessed 1 December 2018. There is evidence of government institutional shareholders in Malaysia actively exercising their voting rights but it is not clear whether they have done so in their capacity as controlling shareholders or minority shareholders; further, the evidence does not differentiate the type of resolutions they have voted, how they have voted (i.e. for or against) and the outcome of their votes. For further analysis, see Chapter 3, Part III(B).

First, transactions involving government entities are outside the scope of the listing rules. In India, transactions between two government companies are exempted.[250] Thus, an RPT entered into between a controlling shareholder (which is a government company) and the listed issuer (if it is also a government entity) does not require the approval of the audit committee or the general meeting. Only board approval of the listed company suffices. Further, in India, no shareholder approval is required for RPTs with wholly-owned subsidiaries[251], even if the transactions are not on normal commercial terms. Thus, a controlling shareholder can enter into RPTs with a wholly owned subsidiary in the group to extract private benefits of control. In Hong Kong, a PRC governmental body will usually fall outside the RPT rules.[252] Thus, if the controlling shareholder is a PRC governmental body, and if it enters into a transaction with the listed company, it will not be subject to the RPT rules. Only board approval suffices. The result is that PRC SOEs that are listed in Hong Kong are exempted from the RPT rules. Considering the extensive evidence of tunnelling in SOEs listed in Hong Kong and the PSUs in India (examined in Part II), exempting the government from the RPT listing rules further exacerbates the problem of extractions of private benefits of control. Finally, in Malaysia, a contract that is awarded by or on behalf of the Government of Malaysia or a State Government to the listed issuer is not regarded as an RPT, even if the government is the controlling shareholder.[253]

Second, transactions of a certain value are exempted from the listing rules. For example, in Singapore, an RPTs whose value is less than 5% does not require shareholders' approval. An RPT whose value is less than 3% does not have to be publicly disclosed. In both types of

[250] SEBI LODR 23(5)(a).

[251] The Companies (Meetings of Board and its Powers) Second Amendment Rules, 2014. General Circular No. 41/2014, Ministry of Corporate Affairs, Government of India.

[252] HKEX LR14A.10.

[253] Bursa Malaysia LR 10.08(11)(i). It is no clear what is envisaged by such contracts.

RPTs, the opinion of the audit committee and the independent financial adviser is not needed at all. In Malaysia, an RPT whose value is less than 5% requires neither the approval of shareholders, the opinion of the audit committee, nor the approval of independent financial adviser. This is similar to the listing rules in Hong Kong. In India, although all RPTs have to be approved by the audit committee and the general meeting, an RPT whose value is less than 10% does not have to be approved by the general meeting. Only approval from the board of directors, over whom the controlling shareholders exercise the power of appointment and removal, is required.

One might argue the solution is to lower the value of RPTs: instead of 5%, we could change the threshold to 3% or even 1%. The solution is not impossible but one has to bear in mind that convening a committee of independent directors, appointing an independent financial adviser, complying with the onerous disclosure rules, and convening a meeting of disinterested shareholders, are all costly to the company. Beyond a certain level, the costs of complying with these requirements will exceed the benefit of entering into the RPTs. It could even deter companies from entering into value-enhancing RPTs. Even if this solution is advisable, two points should be noted. The first is that it is still susceptible to the problems associated with controlling shareholders analysed above. The second is that it is possible to adopt both solutions: lowering the value does not preclude subjecting controlling shareholders to fiduciary duties. It is not an either/or approach.

Third, and finally, the rules on RPTs apply to transactions which relate to the transfer of assets, services, and acquisition of shares, but they do not seem to cover the transfer of opportunity, information or ideas. In this situation, it would seem that no approval from disinterested shareholders is necessary. The reason is because the listing rules are influenced by accounting rules which only recognise transfer of resources, i.e. which excludes ideas, information or opportunity.[254] But extractions of private benefits of control can also take place where there is a transaction between the controlling shareholder and the company that involves the transfer of opportunities, information or ideas.

B. Ex ante: Participative mechanisms

Participative mechanisms refer to the rights of shareholders to attend, speak and vote at the general meeting, and the right to requisition the company to convene general meetings.[255] For example, in all the four common law countries in Asia, shareholders who hold either 5% or 10% of the voting rights can requisition a general meeting.[256] And shareholders in Singapore and Malaysia who hold at least 10% of the issued shares of the company can call for the general meeting.[257] Participative mechanisms also refer to measures to improve shareholder participation in the general meeting, which include but are not limited to allowing them to vote in person or by proxy, and the use of electronic voting. For instance, in India, a law was recently passed to provide electronic voting to shareholders.[258] The objective of these reforms is to increase shareholders' exercise of their voting powers.

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[254] Enriques (n 30) 6.

[255] "Voting with the feet" or "Wall Street Walk" may be loosely classified as a participative mechanism. It involves investors selling their shares: Stuart Gillan and Laura T Starks, "The Evolution of Shareholder Activism in the United States" (2007) 19 *Journal of Applied Corporate Finance* 55. But the impact of this activism in itself on disciplining controlling shareholders is likely to be negligible given the insignificant percentage of shares held by the investors. There appears to be no published research on the correlation between firm value and voting with the feet in the four common law countries in Asia.

[256] HK CO, s 566; SG CA, s 176(1); IN CA, s 100(2); MY CA, s 311(3).

[257] SG CA, s 177; MY CA, s 310(b).

Whether participative mechanisms have been effective depend on whether they have minimised the incidence of extractions of private benefits of control. In short, whether the exercise of voting powers by minority shareholders has the effect of monitoring and possibly disciplining controlling shareholders. That in turn depends on numerous factors: the voting policies of the minority shareholders; whether and the extent to which the minority shareholders in the listed companies in the four common law countries in Asia have actually exercised their voting rights; whether the resolutions are binding; the resolutions on which they have voted; their voting records (i.e. whether they voted for or against a resolution) and the extent in which their voting for or against is affected by conflicts of interest; and what the outcome of the vote was (i.e. whether their votes made a difference to the outcome of the resolution such as whether their vote led to the removal of directors, rejection of RPTs etc or although their vote made no difference to the outcome, the management took note of dissenting votes by the minority shareholders and made certain changes). These are difficult and complex issues. There is limited empirical evidence given that shareholders (save for US mutual funds[259]) are generally not required by law to disclose their voting policies or voting record. Further, listed companies in the four common law countries are not legally required to disclose the identity of the shareholders who voted and the resolutions in which they voted. Moreover, there is limited empirical evidence on how often shareholders have actually exercised their right to requisition meeting or call meeting.[260]

[258] Companies (Management and Administration) Amendment Rules, 2015.

[259] Letter from Alan D Lebowitz, Deputy Assistant Secretary, Department of Labor, to Helmuth Fandl, Chairman of the Retirement Board, Avon Products Inc. (February 23, 1988) (reprinted at 15 Pens. Rptr. (BNA) 391); Investment Company Act of 1940 § 36, 15 U.S.C. § 80a-35 (2012) (stating that an adviser can be held liable for breach of fiduciary duty); Proxy Voting by Investment Advisers, Investment Advisers Act Release No. IA—2106, 68 FR 6585 (February 7, 2003); Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies, Release Nos. 33-8188, 34-47304, IC-25922, 2003 SEC Lexis 3143 (2003).

[260] Cf Yuen Teen Mak and Yi Hong Chew, *The Singapore Report on Shareholder Meetings: Dawn of Activism": Volume 2* (2016) <http://governanceforstakeholders.com/wp-content/uploads/2013/07/Shareholder-Meetings-Volume-2-updated.pdf> accessed 1 December 2018; Yuen Teen Mak and Yi Hong Chew, *The Singapore Report*

However, based on the limited available evidence, two major points have emerged. First, while there is evidence that US institutional investors[261] (who are the minority shareholders in the listed companies in Asia) have exercised their voting powers in relation to director elections and M&A in the companies in Singapore, Malaysia and India[262], there is no conclusive evidence that these shareholders have voted against the resolutions supported by management or the controlling shareholder. One study concluded that when investors (i.e. US institutional shareholders) expect greater expropriation as a result of higher insider control, they will vote against the resolutions (i.e. director elections and M&A) supported by management.[263] In other words, there is greater dissent voting where there is higher rate of expropriation by controlling shareholders. However, the results of the study show that for M&A, Singapore and Malaysia have a lower percentage of dissent voting than the UK (where the listed companies generally do not face the same problem of extractions of private benefits of control by controlling shareholders).[264] As for director elections, India has a lower percentage of dissent voting than the UK.[265] The data generated by the study thus cast doubt on the study's own conclusion that there will be more dissent voting by US institutional shareholders in jurisdictions with more extractions of private benefits of control. This suggests that US institutional shareholders might have voted in line with management recommendations,

on Shareholder Meetings: Dawn of Activism: Volume 3 (2017) <https://docs.wixstatic.com/ugd/c48702_9b302c5fc5574cd2b89d02936db8abc3.pdf> accessed 1 December 2018.

[261] Under US law, the registered investment companies (the managers of mutual funds) and investment advisers (the agents and employees of managers of mutual funds) have to disclose their voting policies and voting outcome (i.e. which resolutions they voted and how they voted): see (n 259).

[262] Peter Iliev and others, 'Shareholder Voting and Corporate Governance Around the World' (2015) 28 *Review of Financial Studies* 2167.

[263] Ibid 2170-2171.

[264] Ibid 2178.

[265] Ibid.

which undermines the claim that participative activism through voting is an effective mechanism to monitor and discipline management and controlling shareholders.

The second point is that other than the evidence of US institutional shareholders' exercise of voting powers discussed above, there is no clear evidence of participative activism by minority shareholders (who are not US institutional investors) that could lead one to conclude that participative activism has reduced extractions of private benefits of control by controlling shareholders. Although there are a handful of examples of minority shareholders who have actively exercised their voting rights (either by voting against management resolutions or requisitioning shareholders' meetings), there is no large scale empirical study of the frequency and effect of participative activism with respect to any particular type of resolution. One cannot therefore conclude from the handful of reported cases of participative activism that minority shareholders in general have actively exercised their voting powers, let alone that the activism has curbed extractions of private benefits of control.

In Hong Kong, there are some instances of US hedge funds playing an active role in going-private transactions in listed companies.[266] One case shows that a US hedge fund acquired more shares in selected companies after the company announced its plans to undertake a going-private transaction, which is a type of squeeze-out.[267] The hedge fund then demanded higher consideration. If the controlling shareholder who is the bidder does not agree to its demands, the hedge fund would holdout by not voting in favour of the privatisation. This strategy minimised extractions of private benefits of control by the controlling shareholder or the bidder. However, apart from this one instance, there seems to be no other cases that demonstrate the role played by minority shareholders in going private transactions in relation

[266] Frank Wong, 'Shareholder Engagement and Activism Under the Radar: Empirical Evidence From Hong Kong (2003-15)-Rethinking Disclosure of Interests Regime' (23 June 2017) <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2725318> accessed 1 December 2018.

[267] See the US hedge fund Elliott Management Corporations involvement in Pacific Century Premium Development Ltd: Wong, ibid, 46.

to the prevention of the extractions of private benefits of control. In addition to going private transactions, there appears to be one case so far in which a hedge fund successfully instigated the appointment of an independent director.[268]

In India, while dissent voting and requisitions by minority shareholders have increased lately,[269] there is no evidence that this trend will continue to rise. In fact, the evidence on the whole is that minority shareholders are generally passive.[270] Further, in view of the concentrated ownership structure of the majority of Indian listed companies, commentators have argued that minority shareholder activism will produce negligible impact on corporate governance.[271]

In Singapore, there is preliminary evidence that suggests that shareholders have become active in exercising their voting powers.[272] For example, in 2015, there were seven requisitioned EGMs by shareholders in six companies concerning the appointment and removal of directors; changes were effected in three out of the seven meetings.[273] In 2016, shareholders in eight companies requisitioned[274] or called for[275] meetings, of which changes were effected

[268] Eric Ng, 'Oasis Seeks Yingde Board Seat to Add Independent Voice Amid Boardroom Tussle' *South China Morning Post* (27 Feb 2017).

[269] Satatya Anand, 'Shareholder Activism in India" (2016) 8 *International Journal of Research in Humanities, Arts and Literature* 11 at 15; India Proxy Season 2017: An Analysis, InGovern Research Services 4-5.

[270] See eg, Jayati Sarkar and Subrata Sarkar, 'Large Shareholder Activism in Corporate Governance in Developing Countries: Evidence from India' (2000) 1 *International Review of Finance* 161, 190; Umakanth Varottil, 'The Advent of Shareholder Activism in India' (2012) 6 *Journal on Governance* 582, 593.

[271] George S Geis, 'Can Independent Blockholding Play Much of a Role in Indian Corporate Governance?' (2007) 3 *Corporate Governance Law Review* 283.

[272] Yuen Teen Mak and Yi Hong Chew, *The Singapore Report on Shareholder Meetings: Shareholders Awaken: Volume 2* (2016); Yuen Teen Mak and Yi Hong Chew, *The Singapore Report on Shareholder Meetings: Dawn of Activism: Volume 3* (2017).

[273] Yuen Teen Mak and Yi Hong Chew, *The Singapore Report on Shareholder Meetings: Shareholders Awaken: Volume 2* (2016) A5.

[274] SG CA, s 176: Shareholders holding not less than 10% of the total number of paid up shares may requisition the directors to convene a meeting.

[275] SG CA, s 177: Shareholders holding not less than 10% of the total number of issued shares can call for a meeting. The difference between s 176 and 177 is that under the former, requisitioning shareholders have to give

in five of the companies.[276] Most of the meetings were concerned with the dismissal and appointment of directors. But there is no evidence that the requisitioning or calling of meetings has led to greater monitoring and disciplining of management and controlling shareholders. The reverse can happen. Shareholders can requisition or call for meetings to pursue their own personal interests which may conflict with those of the company. Commentators have cautioned against requisitioning shareholders appointing themselves or their proxies as directors in order to gain board control and then strip the company of its assets.[277]

In Malaysia, although there is evidence that government institutional shareholders have actively exercised their voting rights, it is not clear whether they have done so in their capacity as controlling shareholders or minority shareholders.[278] That said, the Minority Shareholder Watch Group (MSWG), a public company set up to protect the interests of minority shareholders, has been actively participating in the general meetings.[279] Thus, at the requests of minority shareholders, the MSWG will write letters to the companies to voice concerns prior to, and will ask questions and vote (on behalf of the minority shareholders) at the general

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directors up to 21 days to convene a general meeting and only if the directors refuse to do so that the shareholders can convene the meeting themselves. The company has to pay the requisitionists reasonable costs of convening the meeting. By contrast, under s 177, shareholders do not need to give any timeline to directors and they can call the meeting themselves. But there is no provision stating that the company has to pay the shareholders the cost of holding the meetings.

[276] Yuen Teen Mak and Yi Hong Chew, *The Singapore Report on Shareholder Meetings: Dawn of Activism: Volume 3* (2017) 24.

[277] Ibid 28.

[278] See eg, Investor Stewardship and Future Key Priorities 2016 (Institutional Investor Council Malaysia) 49. We are not concerned with the government's exercise of voting rights as a controlling shareholder because the issue is about whether minority shareholders' exercise of voting rights has curbed extraction of private benefits of control by controllers. The government owns shares either as a controlling shareholder or a minority shareholder in multiple companies. The problem is that the evidence does not distinguish the capacity (controller or minority) in which the government voted. Nor does the evidence disclose whether the votes have led to any outcomes.

[279] Rashid Ameer and Rashidah Abdul Rahman, 'The Impact of Minority Shareholder Watchdog Group Activism on the Targetted Firms' Performance in Malaysia' (2009) 5 *Asian Academy of Management Journal of Accounting and Finance* 67; Siti Sakinah Azizan and Rashid Ameer, 'Shareholder Activism in Family-Controlled Firms in Malaysia' (2012) 27 *Managerial Auditing Journal* 774.

meetings. MSWG provides an important mechanism to discipline controlling shareholders and management. However, there are unresolved conflicts of interest involving MSWG that could considerably reduce its effectiveness as a mechanism to protect minority shareholders and discipline controllers in the government-linked companies (GLCs). For example, doubt has been expressed as to whether the directors of MSWG, who are appointed by or connected to the government (or its affiliate), will do a credible job of monitoring and disciplining the GLCs.[280] The directors of MSWG may be unwilling to act against a listed company that is a GLC should the latter's minority shareholder request MSWG to vote against the resolutions favoured by the board/controlling shareholder of the GLC.

In conclusion, six points can be made: (i) participative mechanisms have been used in certain instances by minority institutional shareholders in the listed companies in the four countries in Asia; (ii) there is a lack of systematic evidence of how often non-US institutional minority shareholders vote, the types of resolutions on which they vote, whether they vote for or against, the outcome of the vote, and the effect of those votes on constraining extractions of private benefits of control by controlling shareholders in each of the four countries; (iii) there is no evidence that minority shareholders have succeeded in displacing the controllers or taking over the company given the concentrated ownership structure of most listed companies in the four countries; (iv) it is generally difficult for minority shareholders to influence board strategies or decisions because directors are appointed and removed by controlling shareholders; (v) except for certain instances, the evidence on the whole suggests that the intuition that minority shareholders have not actively exercised their voting powers is not incorrect; and (vi) in light of points (i) to (v), it is reasonable to conclude that there seems to be no evidence that

[280] Rashid Ameer and Rashidah Abdul Rahman, 'The Impact of Minority Shareholder Watchdog Group Activism on the Targetted Firms' Performance in Malaysia" (2009) 5 *Asian Academy of Management Journal of Accounting and Finance* 67, 77.

participative mechanisms have been proven to effectively curb extractions of private benefits of control by controlling shareholders.

C. Ex post: Controlling shareholders as shadow directors

I have argued above that two of the most important *ex ante* strategies to regulate extractions of private benefits of control by controlling shareholders – the listing rules on RPTs and participative mechanisms - suffer from serious defects. Apart from *ex ante* mechanisms, there are *ex post* strategies. One such strategy for constraining a controlling shareholder's extraction of private benefits of control is to subject him to the same fiduciary duties as directors through the doctrine of shadow directors. Thus, it might be said that there is no need to separately impose fiduciary duties on controlling shareholders. For the purpose of establishing that the controlling shareholder is a shadow director, the claimant has to prove that the controlling shareholder directed the directors to act in relation to the company; those directors acted in accordance with such directions; and they were accustomed so to act.[281]

Three major problems are immediately apparent with the use of shadow directors as a strategy to regulate expropriation by controlling shareholders. First, it is hugely under-inclusive: it does not cover those transactions or actions which the statute, listing rules or the company's constitution specifically require approval from the general meeting, which include but are not limited to the appointment and removal of directors, approval of significant transactions,

[281] *Re Hydrodam (Corby) Ltd* [1994] BCC 161,163; *Tong Tien See Construction Pte Ltd (in liquidation) v Tong Tien See* [2001] 3 SLR(R) 887 [62]; *Moulin Global Eyecare Holdings Ltd v Lee Sin Mei Olivia* [2009] 3 HKLRD 265 at [62] and [63] (judgment reversed by the Court of Final Appeal on other grounds, see [2010] 2 HKLRD 1096; *Cepatwawasan Group Bhd v Tengku Dato' Kamal Ibni Sultan Sir Abu Bakar* [2008] 2 AMR 504 [509] to[512]; *Dr. Joginder Singh Juneja v State of Gujarat* (2017) Indlaw GUJ 1215 [87].

authorisation of breaches of directors' duties and approval of transactions between directors and company; in these situations, unregulated conflicts of interest can arise between the controlling shareholder and the company, as elaborated subsequently in Part IV(A). Nor does it cover the situation when controlling shareholders take up a corporate opportunity as they will not be acting as shadow directors when they learn from a director or a client of the company of a potential business opportunity and pursue the opportunity for themselves.

However, it may be argued that the shadow director mechanism can address the issue of controlling shareholder exerting pressure on the directors to do what he says, particularly in an RPT. This brings us to the second problem. It is difficult for the minority shareholder to prove that the directors were accustomed to act in accordance with the directions given by the controlling shareholder because a one-off direction will not turn a controlling shareholder into a shadow director. It has to be done on a continuing basis; a regular course of conduct has to be demonstrated.[282] Thus, given that the benefit from exerting influence on the director will exceed the cost of being held liable as a shadow director, it is unlikely that the controlling shareholder will be deterred from applying pressure (direct or indirect, subtle or overt) on the board. The final problem is that even if the minority shareholder can prove that the controlling shareholder is a shadow director, the controlling shareholder will escape liability if he discloses to the directors his interest in the transaction prior to the transaction being approved by the board (if approval is required) and provided that he does not vote in approving the transaction (assuming the controlling shareholder is also a director).[283]

[282] *Secretary of State for Trade and Industry v Becker* [2003] 1 BCLC 555; *Ultraframe (UK) Ltd v Fielding* [2005] EWHC 1638 [1270]-[1278]; *Re Unisoft Group Ltd (No 3)* [1994] 1 BCLC 609, 620.

[283] *Imperial Mercantile Credit Association v Coleman* (1873) LR 6 HL 189; HK CO, s 540; SG CA, s 156; MY CA, s 222; IN CA, s 184(2).

D. Ex post: Controlling shareholders as de facto directors

In order for a controlling shareholder to be treated as a de facto director, the minority shareholder must plead and prove that the controlling shareholder took functions in relation to a company which could be discharged properly only by a director; in short, he must have assumed the status and office of a director by participating in the affairs of the company on an equal footing with the other directors.[284] This implies that where the controlling shareholders exercise the powers that can only be exercised by the general meeting (as provided for in the statute, company's constitution or listing rules), namely those that cannot or are not exercised by the office of a director, they cannot be held liable as de facto directors. These powers are significant and substantial: they include but are not limited to: appointing and dismissing directors; altering company's constitution; dictating to overruling the directors (by altering the constitution); approving major transactions; ratifying breaches of directors' duties; approving mergers and acquisitions; approving transactions between the company and the directors; approving executive compensation; altering the status of a company from public to private; and winding up the company. Further, the definition of de facto director will not cover the situation of controlling shareholders exploiting corporate opportunities.

Thus, there is a limit to what the doctrine of de facto directors can do for the purpose of controlling the varying and multiple types of conflicts of interest between the controlling shareholder and the company. Hence, the doctrine of de facto director may be effective only when the controlling shareholder plays an active role in exercising management powers on par with those exercised by the other directors.[285] But the actions of controlling shareholders,

[284] *Secretary of State for Trade and Industry v Hollier* [2007] BCC 11 [68] and [69]; *Re Kaytech International plc* [1999] 2 BCLC 351, 424.

[285] *Secretary of State for Trade and Industry v Jones* [1999] CC 336, 349. Cf (n 313).

which could benefit themselves but at the expense of the company and hence minority shareholders, such as exerting influence on directors, need not rise to the level of assuming the status and functions of a director. Moreover and crucially, where the person acts as an employee, adviser or agent of the company or as a shareholder who is concerned about his investment, he will not be treated as a de facto director.[286] And where there is doubt as to whether the conduct of the person amounts to an assumption of the office of a director or another capacity, the person will not be regarded as a de facto director.[287] For these reasons, the de facto director doctrine is not an effective tool for regulating extraction of private benefits of control by controlling shareholders.

E. Ex post: Bona fide for the benefit of the company as a whole

It may be argued that instead of subjecting controlling shareholders to fiduciary duties, the solution is to extend the duty imposed on shareholders when they alter the articles to all other exercises of formal and informal power by controlling shareholders. The duty is to act bona fide for the benefit of the company as a whole, as stated in *Allen v Gold Reefs*. However, the problem is that the *Allen v Gold Reefs* test is diametrically opposite to the directors' fiduciary duty to act in good faith in the best interests of the company. The *Allen v Gold Reefs* test only requires shareholders not to deliberately harm the company's interests insofar as the

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[286] *Secretary of State for Trade and Industry v Hollier* [2007] BCC 11.

[287] *Re Richborough Furniture Ltd* [1996] 1 BCLC 507 at 524; *Re Mumtaz Properties Ltd, Wetton v Ahmedi* [2012] 2 BCLC 9 [30]; *Re UKLI Ltd, Secretary of State for Business, Innovation and Skills v Chohan* [2013] EWHC 680 [38].

harm is due to the lawful exercise of their voting powers.[288] The test prohibits shareholders from intentionally causing harm. But if the harm is an effect or consequence of their lawful exercise of their right to vote, the shareholders will not be liable. Lawful here refers to compliance with the statute, company's constitution, listing rules or other applicable laws. The English Court of Appeal[289] has confirmed that the *Allen v Gold Reefs* test allows shareholders to vote as they wish, based on their own interests, if their assertion that they have voted bona fide for the company's benefit is not impugned. And it is most unlikely to be impugned because the threshold is very low: it is not unreasonableness but irrationality; in other words, as long as a rational or plausible reason can be given for the shareholders' voting decision, it will not be impugned.[290]

By contrast, directors' fiduciary duty to act bona fide in the company's best interest requires directors to affirmatively advance the company's interests. It is necessary but insufficient that directors do not intentionally harm the company. They have to take positive steps to protect and promote the company's interests, unlike the *Allen v Gold Reefs* test.

The *Allen v Gold Reefs* test should not be applied to the exercise of powers by controlling shareholders for the following reasons. The *Allen v Gold Reefs* test is contrary to the principle that the general meeting is an agent of the company and thus owe fiduciary duties to the company. When shareholders vote to decide whether to approve major transactions, to appoint or remove directors, to approve transactions between the company and directors, to change the status of a company from public to private, to approve executive compensation, or to direct directors to take or refrain from taking certain action, they are exercising corporate

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[288] Richard Nolan and Matthew Conaglen, 'Good Faith: What Does it Mean for Fiduciaries, and What Does it Tell Us About Them' in Matthew Harding and Elise Bant (eds), *Exploring Private Law* (CUP 2010) 329.

[289] *Citco Banking Corporation NV v Pusser's Limited* [2007] UKPC 13; [2007] BCC 205 [26], [27].

[290] *Shuttleworth v Cox Bros & Co (Maidenhead) Ltd* [1927] 2 KB 9, 18; David Kershaw, *Company Law in Context: Text and Materials* (2nd edn, OUP 2012) 658.

power. The decisions made by the shareholders bind the company and alter the company's legal position. For example, with respect to major transactions, when shareholders vote to decide whether to dispose of the company's assets, they are not entitled to act in their own interests for these assets belong to the company, not them. We are reminded that a sole shareholder or the whole body of shareholders 'cannot validly consent to their own appropriation of the company's assets for purposes which are not the company's.'[291] Given that shareholders are not the owners, principals, or organs, nor are they the residual claimants as subsequently explained in Chapter 4 (except in the rare situation of voluntary winding up), there is no basis for allowing them to vote solely in their self-interests as long as they do not deliberately inflict harm on the company, which is essentially what the *Allen v Gold Reefs* test entails. Instead, because controlling shareholders have significant discretionary powers over the company, which are difficult to monitor and control, and which makes the company particularly vulnerable, it is inapposite that controlling shareholders should simply be required to only avoid any intentional infliction of harm on the company, which is what is required by the *Allen v Gold Reefs* test.

F. Ex post: Oppression/unfair prejudice

It may be said that instead of subjecting controlling shareholders to fiduciary duties, the mechanism of oppression (as is known in Singapore, India and Malaysia) or unfair prejudice (as is known in Hong Kong) can be used to regulate extractions of private benefits of control.

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[291] *Prest v Petrodel Resources Ltd* [2013] UKSC 34; [2013] 2 AC 415 [41].

In the four countries in Asia, provided that the shareholder can show that his interests have been unfairly prejudiced or oppressed by the company's affairs, the court has wide discretion regarding the remedy that it can award (including ordering the shares of the aggrieved shareholder to be bought out, and ordering certain action to be taken or certain action to be discontinued).[292]

There are however three reasons why the mechanism of oppression/unfair prejudice will not be effective. First, the objective of the oppression/unfair prejudice remedy is not to curb extractions of private benefits of control that arise from conflicts of interest. Rather, the objective is to protect shareholders from unfair prejudice or oppression. These objectives are not necessarily coterminous. In short, the oppression remedy is intended to address personal wrongs rather than corporate wrongs. Second, there is a lack of clarity and certainty in determining what actually constitutes 'unfairness' in oppression. Third and finally, there is difficulty with using the oppression/unfair prejudice mechanism in the context of a listed company.

Regarding the first point, consider the following example, the facts of which are taken from two different cases. In the first case[293], the controlling shareholder who was also a director used the company's funds to pay for his own personal expenses. He caused the company to issue low dividends, so that he can increase his annual bonus. In the second case,[294] the controlling shareholder who was also a director also used the company's funds to pay for his own personal expenses. But unlike the first case, the minority shareholder had been receiving substantial dividends from the company; his claim was not supported by other disinterested shareholders; and he rejected the offer to buy out his shares. Instead he insisted that the

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[292] See eg, SG CA, s 216; MY CA, s 346; IN CA, s 246(1), 242; HK CO, s 724.

[293] *Low Peng Boon v Low Janie* [1999] 1 SLR 761.

[294] *Re Kong Thai Sawmill (Miri) Sdn Bhd* [1978] 2 MLJ 227, 229.

company be wound up. In the first case, the court held that there was oppression as there was commercial unfairness whereas in the second, the court held that there was no oppression. In both cases, there was diversion of corporate assets to the controlling shareholder; there were clearly extractions of private benefits of control. Yet, the controlling shareholder was liable in the first but not the second. The reason is because the additional facts in the second case led the court to take the view that there was no commercial unfairness to the minority shareholder. This case showed that (1) even if there were extractions of private benefits of control or expropriation of company's assets, it would not necessarily amount to oppression; and (2) oppression is not the appropriate tool to regulate extractions of private benefits of control.

The two cases demonstrate that the main objective of the oppression/unfair prejudice remedy is not to regulate extractions of private benefits of control or conflicts of interest by controlling shareholders; rather it is to protect minority shareholders by giving them personal remedies for the wrongs committed by the directors or management against the former (although these wrongs stem from conflict of interest). That is why, as illustrated by the court's reasoning in the two cases above, extractions of private benefits of control that arise from conflicts of interest do not necessarily amount to oppression. The aim of the oppression remedy is not so much to address corporate wrongs by controlling extractions of private benefits of control and conflicts of interest, but rather to give a personal remedy to minority shareholders who are unfairly and adversely affected by the actions of majority shareholders. If that is the case, then oppression/unfair prejudice is not an appropriate or effective mechanism to regulate extractions of private benefits of control that arise from conflicts of interest involving controlling shareholders.

Further, while the delinquent controlling shareholder in the two cases committed the same act i.e. extracted private benefits of control from the company, the controller in the first case was held to have caused unfairness to the minority shareholder but not the other. This brings us to the second point, which is that even if it were appropriate to use the oppression mechanism to regulate tunnelling by controllers, it is hampered by uncertainty as courts have not yet set out any clear criteria as to what is meant by 'unfairness' in the oppression action. The test used to determine whether there is oppression is that of 'commercial unfairness'[295], under which two limbs must be established: (1) the defendant's misconduct must be a breach of an understanding between the members, and (2) the breach must have resulted in unfairness to the complainant member.[296] The court has provided guidance on the first[297] limb but not the second. The latter depends on how courts construe the facts. However, if controlling shareholders were subject to fiduciary duties, they would be held liable in both of the cases discussed above, independent of whether it is commercially fair or unfair to the minority shareholder. The fiduciary duty strategy already sets out some guidelines or standards, namely, that the controlling shareholder is not permitted to put himself in a position of actual or potential conflict of interest.[298] Should he obtain any profits from this position, he would generally be required to disgorge them. As a strategy to curb extractions of private benefits of control, it is much more effective than oppression.

Third and finally, even if oppression were an appropriate tool to regulate extractions of private benefits of control, it would be difficult to utilise it in the context of a listed company. In order for a minority shareholder to succeed, she usually needs to show that there is a breach of an informal, personal agreement or informal understanding between the parties that the affairs of the company are to be conducted in a certain way which makes it inequitable to

[295] *Over & Over Ltd. v Bonvest Holdings Ltd* [2010] 2 SLR 776.

[296] *Ng Sing King v PSA International Pte Ltd* [2005] SGHC 5.

[297] *Ebrahimi v Westbourne Galleries Ltd* [1973] AC 360; *O'Neill v Phillips* [1999] 1 WLR 1092; *Over & Over Ltd. v Bonvest Holdings Ltd* [2010] 2 SLR 776.

[298] Potential would mean in the context of pursuing an opportunity whether it is outside or within the scope of the company's business.

restrict the petitioner to her legal rights.[299] But it is difficult for a minority shareholder in a listed company to prove that.[300] In Singapore, there appears to be only one case in which a minority shareholder in a listed company has successfully proven that she has legitimate expectations that the company's affairs should be conducted in certain way, which expectations arose out of a relationship of mutual trust and confidence that subsisted when the company was set up.[301] In Hong Kong, there appears to be one successful case of oppression in a listed company. This is not because the petitioner proved there was an informal personal agreement between it and the company; rather, the petitioner showed that in obtaining a listing on the stock exchange, the company must be taken to have made an implied promise to the shareholders that it has done so for the shareholders' benefit, such that should the company breach the listing rules, the company would prejudice the shareholders' interests.[302] There appears to be two cases on oppression involving listed companies in India[303] and one in Malaysia[304], none of which was successful.

Having showed the deficiencies in the current and potential *ex ante* and *ex post* strategies for regulating extractions of private benefits of control, I now turn to the second justification for imposing fiduciary duties on controlling shareholders, namely, that there are

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[299] *O'Neill v Phillips* [1999] 1 WLR 1092; *Wong Man Yin v Ricacorp Properties Ltd* (2003) 6 HKFAR 265; *Lim Swee Khiang v Borden Co (Pte) Ltd* [2006] 4 SLR(R) 745.

[300] It is possible for a minority shareholder such as an institutional shareholder to have such a personal dealing but it would likely take the form of a formal agreement on an arms-length basis given the resources and clout of the institutional shareholder.

[301] *Tan Choon Yong v Goh Jon Keat* [2009] 3 SLR(R) 840.

[302] *Luck Continent Ltd v Cheng Chee Tock Theodore* [2013] 4 HKLRD 181.

[303] *Morgan Ventures Limited v Blue Coast Hotels and Resorts Limited* [2010] 155 Comp Cas 431 (petition unsuccessful because the petitioner made a false averment that he had the support of more than 100 members, as the statute requires that the oppression remedy can only be invoked provided that there are not less than 100 members of the company in support of this petition); *Union of India (UOI) Vs. Satyam Computer Services Ltd* [2009] 148 Comp Cas 252.

[304] *Kang Choon Leu @ Kang Chee Sim v Wintoni Group Berhad* [2016] AMEJ 1264 (petition unsuccessful because petitioner's interests were not affected; only the corporate interest was).

conflicts of interest between the company and the controlling shareholder which could give rise to extractions of private benefits of control by the latter that are not regulated by the current law.

IV. Conflicts of interest and extractions of private benefit of control not regulated by the law

RPT is only one manifestation of conflict of interest that can give rise to extraction of private benefit of control. There are many other types of actual and potential conflicts of interest that are outside the scope of the current law. They arise from actions or transactions where the interests of the controlling shareholders conflict or may possibly conflict with those of the company. They can be broadly divided into two categories: when controlling shareholders exercise their voting powers and when they do not exercise voting powers but instead exert influence on the company. In other words, when they exercise formal (i.e. corporate) powers and informal powers. Controlling shareholders can extract private benefits of control in those two types of situations. In light of the fact that the majority of listed companies in the four countries are dominated by controlling shareholders, they exercise considerable power in those types of situations.

A. Category 1: Exercise of voting (i.e. corporate) powers

1) *Appointment and removal of directors*. As examined earlier, any director can be removed without cause by a simple majority despite anything contrary to the company's

constitution.[305] A director who defies a controlling shareholder can be easily removed. No reasons need to be given. A controlling shareholder can appoint or dismiss directors solely for his own benefit, and even if doing so is to the detriment of the company and minority shareholders. For example, a controlling shareholder can refuse to appoint a director who is a threat to the controller although it would be in the company's interests to make the appointment.[306] Also, a controlling shareholder can easily remove or even threaten to remove the independent directors who do not recommend the approval of the RPT. Or a controlling shareholder can fire or threaten to fire a director who pursues a strategy or takes on a transaction to which the controlling shareholder objects. Thus, directors who are appointed by the controlling shareholder are likely to seek the views of and even obtain the informal approval of controlling shareholder before making any important decisions (even if formal approval is not required). Due to the lack of restrictions on the controlling shareholder's power to appoint and remove directors, it remains arguably the most potent weapon for controlling shareholder to advance his own personal agenda.

2) *Dictate to or overrule the directors*. By altering the articles (which requires special resolution), a controlling shareholder can dictate to the directors, overrule the directors' decisions, restrict or remove power from directors. There is no restriction on alteration

[305] See MY CA, ss 203(1) and 206 regarding appointment and removal of directors respectively; IN CA, ss 152 (2) and 169 for appointment and removal of directors respectively.

[306] For example, a 20% shareholder of a listed company (MRO-TEK Realty) in India requisitioned a postal ballot to propose his appointment to the board as a non-executive director. This was because the company entered into a controversial joint development agreement with an unrelated party to develop a land owned by the company. The unrelated party then became the new promoter (i.e. controller) of the company. However, the terms of the agreement were highly favourable to the new promoter but against the company's best interests. Unsurprisingly, the promoter voted against the appointment although more than 80% of the non-controlling shareholders voted in favour of it. See 'Battle for B'luru Property Lands at Govt's Doorstep' *Times of India* (19 Sep 2016); India Proxy Season 2017: An Analysis, InGovern Research Services 7 <http://www.ingovern.com/wp-content/uploads/2017/11/India-Proxy-Season-2017.pdf> accessed 1 December 2018.

except that it must be done bona fide for the benefit of the company as a whole. The problem with the *Allen v Gold Reefs* test as discussed earlier is that shareholders only have to avoid deliberately harming the company. Shareholders are not required to act affirmatively in the company's best interests. This is a very low threshold that can be easily overcome. Thus, the alteration is unlikely to be invalidated. Moreover, courts are traditionally reluctant to intervene in the internal management of the company (particularly if the problems can be subsequently rectified by the general meeting). Finally, save for one case in Hong Kong[307], there appears to be no reported cases where the alteration has been challenged in the other three countries in Asia.

3) *Directing directors to take action/binding recommendation*. Even without altering the articles, the default rule in Hong Kong is that shareholders can by special resolution order directors to take or refrain from taking specified action.[308] The default rule does not impose any restriction on the shareholders when they do so, except that the resolution 'does not invalidate anything that the directors have done before the passing of the resolution.' And there appears to be no judicial or statutory guidance on the circumstances in which shareholders can exercise such power. Thus, a controlling shareholder can order directors to take certain action that benefits him but is at the expense of the company and other shareholders. In Malaysia, shareholders can make a recommendation to the board on matters affecting the company's management that is binding on the company.[309] The shareholders can make such recommendation either

[307] *China Shanshui Cement Group Ltd v Zhang Caikui* [2016] HKEC 116 (where an interlocutory mandatory injunction was granted for a challenge of unlawful amendment of articles of associations).

[308] Schedule 1 Model Articles for Public Companies Limited by Shares, s 3(b) (but note that the resolution 'does not invalidate anything that the directors have done before the passing of the resolution').

[309] MY CA, s 195.

through a special resolution or if the right to make recommendation is provided for in the constitution. But the recommendation has to be 'in the best interests of the company.'[310] This is an important restriction but there appears to be no case law or statutory guidelines on what is meant by that phrase. It is also unclear who is allowed to decide whether the recommendation is in the company's best interests (i.e whether the directors or the shareholders who make the recommendation) and what the test for the company's best interests is.[311] If it is the shareholders who decide, and if the test is similar to that in *Allen v Gold Reefs*, (namely, the restriction imposed on shareholders when they alter the articles), then it is unlikely to be effective in curbing extractions of private benefits of control because the controlling shareholder can easily come up with a plausible reason for directing directors to take certain action, although the real underlying reason is to extract private benefits of control. If it is the directors who decide, then there is a risk that should they defy the controlling shareholders by asserting that the recommendation is not in the company's best interests, they could be threatened with removal or removed.

4) *Exercise management power*. Shareholders can allocate and exercise management powers to themselves as long as these powers are provided for in the statute or the company's constitution. In other words, directors can exercise all management powers except those that have been allocated to the shareholders in the statute or the company's constitution. If those powers are not provided for in the company's constitution when the company was incorporated, shareholders could, on an ordinary and natural

[310] MY CA, s 195(3).

[311] Aiman Nariman Mohd-Sulaiman and Shanty Rachagan, 'Shareholder Primacy, Controlling Shareholders and Malaysia's Companies Act 2016' (2017) 17 *Journal of Corporate Law Studies* 203, 208-210.

construction of the statutory provision, arguably by special resolution create powers for themselves or take back the powers that were originally allocated to the directors for themselves.[312] Even if shareholders are subject to the same fiduciary duties as directors when they exercise management powers, it begs the question as to why these duties do not apply to them when they exercise other types of power that are reserved for them in the statute but which could have far greater material and adverse effect on the company and other shareholders. These powers include but are limited to approving significant transactions, approving M&A, changing the status of a company from public to private, and winding up the company.[313]

5) *Major transactions*. In the four countries in Asia, any transaction that exceeds certain value has to be approved by the general meeting under the listing rules. In Hong Kong, any transaction that is equal to or exceeds 25% of the prescribed asset, profit, revenue or consideration ratio requires an ordinary resolution. In Singapore, any transaction that exceeds 20% of the net asset, net profit or the value of the consideration compared to the issuer's market capitalisation requires an ordinary resolution. In Malaysia, the percentage threshold is 25% and an ordinary resolution is needed.[314] In India, any

[312] Cf *Lee v TYC Investment Pte Ltd* [2015] SGCA 40 (holding that the shareholders have reserve or residual management power only where the board is unwilling or unable to do act (at [28]). Further, the court held (at [27]) that shareholders cannot *ordinarily* control the board's exercise of such powers by passing a resolution to override or reverse it).

[313] One may query whether shareholders who exercise management powers on par with directors will be treated as de facto directors. Note that first, the de facto director doctrine does not and is not intended to cover the situation in which shareholders exercise powers (whether management or otherwise) that are authorised by the statute, company's constitution or listing rules. It is precisely because the statute or the constitution does not authorise the acts of the person in question that the de facto director doctrine is needed to hold him liable where he has assumed the office and functions of a director. Second, if shareholders were de facto directors when they exercise management or quasi-management powers, then shareholders who vote to approve or reject major transactions (regulated by the listing rules) which is a quintessential management power will also be treated as de facto directors. But this is not the law and no one seems to have argued that it ought to be the case.

[314] Bursa Malaysia LR 10.07.

transaction that exceeds 20% of the net worth or generates 20% of the total income requires a special resolution, not ordinary resolution (unlike the other three countries).

To begin, deciding whether to make disposals, acquisitions, loans, guarantees, entering into leases or joint ventures usually fall within the scope of management powers of board of directors who have to exercise these powers in accordance with the fiduciary rules. However, once the value of these transactions exceeds a certain amount, the power is transferred to the shareholders who alone are authorised to make the decision. However, shareholders are not subject to any common law duties, let alone fiduciary duties, when they make such critical decisions. It is remarkable that the duty to act in the company's best interests applies to the board's decision as to whether to approve transactions whose value is less than 20% but it no longer applies (to shareholders) when the value exceeds 20%, the latter of which could have far more material and adverse impact not only on the shareholders but the company and its other stakeholders. Moreover, in light of the fact that major transactions often (but not always) involve dealing with the company's property, it is odd that shareholders' decision is not subject to the fiduciary duty to act in the company's best interests.

The listing rules impose restriction on shareholders who have an interest in the transaction but it is insufficient to prevent extractions of private benefits of control by the controlling shareholder when they vote to approve or reject the major transactions. The restriction is (i) disclosure of interest (in Singapore[315] and Malaysia[316]) only or (ii) disclosure of interest and abstention of voting (in Hong Kong[317]). India requires neither

[315] SGX LR 1014, 1010.

[316] Bursa Malaysia LR Appendix 10B(24).

disclosure nor abstention. But unlike the other three countries, a special resolution not ordinary resolution is required.

The restriction imposed on shareholders in Singapore and Malaysia (i.e. disclosure of interest) is not sufficient to prevent extractions of private benefits of control by controlling shareholders. Consider the following example, the facts of which are taken from a real case.[318] A shareholder invested $7 million in a company in exchange for 40% of the company's common shares and secured notes. As a result, he would fall within the definition of a controlling shareholder in all the four countries in Asia. The controlling shareholder subsequently converted the secured notes into preferred shares which entitled him to a liquidation preference of $17 million in the event that the company sells most of its assets. Two years later, the controlling shareholder acquired shares in the company thereby owning slightly over 50% of the common shares. The controlling shareholder then exerted pressure on the board to cause it to sell most of the company's assets to a third party for $17.3 million. Given that this transaction required the approval of an ordinary resolution, it was easily passed by the general meeting, which comprised the controlling shareholder. This amount was then used to pay for the controlling shareholder's liquidation preference, to the detriment of the company and the minority shareholders as the company was reduced to an empty shell.

Consider another example. The controlling shareholder of a listed technology company in Malaysia persuaded the board that the company should enter into a joint venture agreement with a technology company in China, the consideration of which exceeds 25% of the net assets of the Malaysian company. The controlling shareholder

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[317] HKEX LR 14.46. 'Material interest' is whether the shareholder or his close associate (i.e spouse or child) is a party to the transaction or whether the transaction confers a benefit to the shareholder or his close associate that is not available to other shareholders: HKEX LR 2.27.

[318] *DiLillo v Ustman Technologies, Inc.* 2001 WL 1469057 (Cal. Ct. App Nov. 19, 2001); Iman Anabtawi and Lynn Stout, 'Fiduciary Duties for Activist Shareholders' (2008) 60 *Stanford Law Review* 1255, 289.

owns no shares in the Chinese company but another company of which his relative is a controlling shareholder has a business relationship with the Chinese company. His relative's company is likely to gain more business from the Chinese company if the joint venture goes through. Some members of the board are highly sceptical that this joint venture will benefit the Malaysian company but the directors appointed by the controlling shareholder support him. In the end, the controlling shareholder discloses his interest and votes in favour of this joint venture. As only an ordinary resolution is required, the resolution was passed. The joint venture subsequently turned out to be a failure, causing massive losses to Malaysian company, but the company of the controlling shareholder's relative reaped handsome profits.

Consider one final example. A shareholder is a controlling shareholder of Company A and Company B, both of which are rivals. It is in the best interests of Company A and Company B to have the assets of a non-profitable business within each of the respective company to be sold to a third party. But there is only one buyer available. Should the controlling shareholder favour Company A or Company B by approving the sale? Provided that the controlling shareholder discloses his interests in both companies to each of them, he can vote as he pleases with either regard for only one company or with no regard for either. Thus, he can privilege the interests of Company A and its shareholders over Company B by voting in favour of the sale in Company A and voting against the sale in Company B.

The first and second examples mentioned above illustrate the fact that the law regulating major transactions in Singapore and Malaysia does not constrain extractions of private benefits of control by the controlling shareholder (whether directly in the first example or indirectly in the second). The third example shows that the controlling shareholder's action can benefit one company, but at the expense of the other company and its shareholders.

In India, not only can a controlling shareholder who has an interest in the transaction vote (unlike Hong Kong), but he need not disclose his interest at all (unlike Singapore, Malaysia and Hong Kong).

Hong Kong's regulation is stricter than the other three countries as the interested shareholder not only has to disclose his interest, but has to also abstain from voting. However, the problem is that even if the controlling shareholder complies with these restrictions, he can still exert pressure on the other non-controlling shareholders to vote in a way that is desired by the controller, and it would be difficult for these non-controlling shareholders to refuse if they have business relationships with the controller or the company.

6) *Authorisation and ratification.* The general meeting can generally relieve a director from liability by authorising the conflict of interest (if full and frank disclosure is given) or by ratifying the breach of fiduciary duties by the director.[319] The delinquent director could be the controlling shareholder himself, a family member of the controller in the case of a family-owned company, or a nominee of the controlling shareholder in the case of a GLC/SOE. The problem is that in the four countries in Asia, there appears to be no legal restriction on shareholders' ability to authorise conflicts of interest or other types of directorial breaches. Thus, a controlling shareholder can vote to give advance consent to an action (which would otherwise result in a breach of director's duty) that a director who is his family member or nominee is planning to take. If the controlling shareholder is also the director, he is not barred from voting in the general meeting to

[319] See eg *Regal (Hastings) Ltd v Gulliver* [1967] 2 AC 134, 150.

authorise his own actions. Such actions taken by him (as a director) or other directors (who are his family members or nominees) can include but are not limited to pursuing corporate opportunities, engaging in businesses that compete with the company, or entering into value-decreasing RPTs (that are outside the scope of the listing rules). These actions will benefit (whether directly or indirectly) the controlling shareholder, but are detrimental to the company.

In relation to ratification of breaches of director's duties, the problem is that under the laws of Singapore, Malaysia and India[320] which are based on English common law, the controlling shareholder is not precluded from ratifying any breaches of duties by a director who is his family member or nominee, provided that the ratification is not related to the disposal of the company's assets that infringes the capital maintenance rule to the creditors' detriment[321], and provided that they are not related to acts when the company is actually or near insolvent as creditors' interests are paramount.[322] Thus, with the exception of these two provisos[323], where a director who is a family member or nominee of the controlling shareholder profits from his position as a director (such as by exploiting a corporate opportunity, using the company's property to advance his own interest or engaging in a business that competes with the company), the controlling shareholder is not barred from ratifying the delinquent director's breach of duty.

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[320] Unlike the other three countries, ratification in Hong Kong is governed by the statute: s 473 of the HK CO states that the vote of the delinquent director himself or an entity associated with the director (which includes his family member) is to be disregarded.

[321] See eg *Re Exchange Banking Co, Flitcroft's Case* (1882) 21 Ch D 519; *Re Halt George* (1964) Ltd [1982] 3 All ER 1016.

[322] *West Mercia Safetywear Ltd v Dodd* [1988] BCLC 250, approving *Kinsela v Russell Kinsela Pty Ltd* (1986) 4 ACLC 215, 223.

[323] It has been said that shareholders cannot ratify acts which amount to the misappropriation of 'money, property or advantage which belong to the company or in which the other shareholders are entitled to participate', which is known as fraud on the minority (or more accurately put, fraud on the company). But if the wrongdoing director who is also the shareholder abstains from voting to ratify his wrongdoing, it has been said that there will not be a fraud on the minority and the ratification is valid: Brenda Hannigan, *Company Law* (4th edn, OUP 2016) 541-2.

B. Category 2: Exercise of powers other than by voting

7) *Dividend payouts*. Controlling shareholders can influence the directors to declare huge dividend payouts.[324] The payouts are substantial. For example, in one study, the ratio of dividend payout to cash compensation for CEO who is also the chairman is 14:1.[325] And the ratio for the average chairman is 18:1.[326] The evidence shows that the substantial payouts reflect huge extractions of company's resources to the benefit of the controlling shareholders or their associates.[327]

8) *Existing business relationships with the company*. Suppose the listed company enters into a contract with the controlling shareholder to provide certain services. The latter then subsequently breaches the contract. The controlling shareholder could exert influence on the directors to cause them not to take legal action against him. Or even without any influence from the controlling shareholder, the directors may decide not to sue him, in part because their reappointment and dismissal depends on the controller. But suppose the controlling shareholder did not breach the contract. The controlling shareholder however wants to continue to be the sole supplier although it may be more cost efficient for the company to turn to other suppliers. The controlling shareholder

[324] See eg, Chen (n 35) 446.

[325] Ibid.

[326] Ibid.

[327] Ibid 433 and 445.

can pressurise the board not to engage other suppliers. In any event, the board may be reluctant to antagonise the controlling shareholder by terminating its existing supply agreement with the latter and enter into new agreement with a different supplier.

Consider another example. The board of directors of an aircraft company is considering whether to sell some of its aircrafts as its current business of leasing these aircrafts is no longer profitable. Thus, it is in the company's best interest to sell the aircrafts. But selling these aircrafts would mean that the company no longer requires maintenance of these aircrafts, the service of which has been provided by another company controlled by the controlling shareholder. This means that the latter company (and hence the controller) could potentially lose an important source of income. The controlling shareholder exerted influence on the directors and as a result, they abandon the plan to sell the aircrafts.

The final example is where the controlling shareholder is a creditor of the company. Suppose it is more efficient for the company to breach the credit agreement and pay the damages to the controlling shareholder, instead of continuing to pay the hefty interest to the controlling shareholder. If the controlling shareholder places more premium on the credit agreement, he may cause the company not to breach the contract by exerting influence on the board. Another situation is that if the controlling shareholder is concerned whether the company is able to pay back the interest, he could dissuade the board not to engage in other transactions which are risky but could be very profitable for the company.

9) *Exploitation of corporate opportunities*. A director will be in breach of his fiduciary duties if he pursues an opportunity that he encounters in his course of directorship even if the company is unwilling or unable to pursue it, unless he obtains consent from the

general meeting.[328] But replace the director with controlling shareholder and fiduciary duties no longer apply. Under the current law, a controlling shareholder is not prohibited from exploiting an opportunity that he learns from the directors or the company's clients. No consent from the company (whether the board or the disinterested shareholders) is needed. Suppose the controlling shareholder discovers that the board is deliberating whether to make a strategic investment in another company. Realising how lucrative this opportunity is, he quickly makes the investment, thereby depriving the company of this opportunity. Under the law, neither disclosure to, nor consent from, the company is required before he exploits the opportunity. He makes a handsome profit out of it. He is not required to disgorge the profits under the common law or listing rules.

10) *Investments in competing companies*. Unless prior consent is sought from both companies, a director will be in breach of his fiduciary duty if he holds directorships in two competing companies given that there is real sensible possibility of conflict. But there is no law prohibiting a person from being a controlling shareholder in two competing companies. This is problematic given that (i) the statute stipulates that many crucial decisions could only be made by shareholders; (ii) the vote of the controlling shareholders is often pivotal to the outcome (depending on the percentage of votes he holds and whether an ordinary or special resolution is required); (iii) controlling shareholders wield tremendous amount of influence over the board particularly in

[328] *Regal (Hastings) Ltd v Gulliver* [1967] 2 AC 134; *Kishimoto Sangyo Co Ltd v Oba* [1996] 2 HKC 260, 267; *Swiss Butchery Pte Ltd v Huber Ernst* [2010] 3 SLR 813 [7]-[8]; MY CA, s 214(1)(b) for the no-conflict and no-profit rule. *Pharmmalaysia Berhad (In Receivership) v Dinesh Kumar a/l Jashbhai Nagjibha Patel* [2004] 6 AMR 661 at [704] and [707]; IN CA, s 166 (4) for the no-conflict and no-profit rule. *Kishore Kundan Sippy v Samrat Shipping and Transport Systems P Limited* 2003 Indlaw CLB 7.

family-owned companies and SOEs/GLCs in the four countries in Asia; and (iv) controlling shareholders are likely to have access to material non-public information which they could use to their benefit. Although insider trading law prohibits shareholders from trading on such information, corporate law does not prohibit controlling shareholders from using the information in certain ways to gain an unfair advantage, which will be to the detriment of the company and minority shareholders.

For example, a shareholder owns 35% in Company A and 51% in Company B. He will be considered, with respect to Company B, a controlling shareholder in all the four countries, and with respect to Company A, a controller in Singapore, Malaysia, Hong Kong (and probably in India). He learns from one of the directors of Company A that the board is in confidential discussion with Company C regarding a potentially lucrative transaction. (He is neither a shareholder of nor is he related to Company C and so the RPT rules are not triggered.) He then informs the board of Company B that Company C is talking to one company (without identifying it) about a potential deal. The board of Company B sees the merits of the potential transaction and offers better terms to Company C. Unsurprisingly, Company C eventually enters into the transaction with Company B but rejects the offer from Company A. This benefits Company B but not Company A. One may wonder why the controlling shareholder would disclose the information to Company B because being a shareholder of Company A (he owns 35%), he would also stand to lose if Company A's deal with Company C falls through. The reason is simple. He stands to gain more in terms of the increase in share price if the deal is between Company B and C in light of his higher shareholding in Company B. Corporate law as it stands does not prevent the controlling shareholder from engaging in this sort of arbitrage. Nor does it prohibit the controlling shareholder, who is neither a director nor employee of Company A, from disclosing the confidential information to

Company B. Another reason why the controlling shareholder would disclose the information to Company B is that he plans to reduce his shareholding in Company A in due course. Regardless of the reasons, the action of controlling shareholder adversely affects the interests of Company A and the other shareholders. Nevertheless, he is not liable under existing law.

Consider another example. A person is a controlling shareholder in both Company A and B who are rivals. Both companies are bidding to acquire Company C. The controlling shareholder has access to material non-public information of Company A and B. If he discloses certain information about Company A to Company B, that would increase the chances of Company B succeeding in the bid, to the detriment of Company A, and vice-versa. Corporate law does not prohibit the controlling shareholder from disclosing such information.

Having examined the second justification for the imposition of fiduciary duties that are not regulated by the existing law, i.e. conflicts of interest that can give rise to extractions of private benefits of control, I now turn to the third and last justification.

V. Justifications for imposing fiduciary duties on directors should also apply to controlling shareholders

There are three justifications for imposing fiduciary duties on directors that should also apply to controlling shareholders. The first relates to self-serving motives of directors, the second information asymmetry between the director and the company, and finally, incomplete contracts.

A. Opportunism

Regarding the first justification, the concern is that directors may exercise the discretionary powers conferred on them, that will affect the interests of the company, for their own benefit.[329] Williamson puts it compendiously as 'opportunism' which he defines as 'self-seeking interest with guile.'[330] In one of the most widely cited dicta, Lord Herschel said in *Bray v Ford* that: 'I regard it rather as based on the consideration that, human nature being what it is, there is danger, in such circumstances, of the person holding a fiduciary position being swayed by interest rather than by duty, and thus prejudicing those whom he was bound to protect.'[331] Thus, the law has to step in to reduce or remove the propensity or temptation of directors to prefer their interests to those of the company.

Similarly, controlling shareholders who are given discretionary corporate powers that can affect the interests of the company can exercise these powers for their own interests at the company's expense. To recap, these discretionary corporate powers include but are not limited to appointment and removal of directors; alteration of company's constitution; approval of

[329] Paul B Miller, 'The Fiduciary Relationship' in Andrew S Gold and Paul B Miller (eds), *Philosophical Foundations of Fiduciary Law* (OUP 2014) 63.

[330] See Oliver E Williamson, *Markets and Hierarchies: Analysis and Antitrust Implications* (Macmillan 1983) 47.

[331] [1896] AC 44, 51. See also *York Buildings Co. v Mackenzie* (1795) 8 Bro PC 42, 63, 3 ER 432, 446.

major transactions; authorisation of transactions that would otherwise amount to a breach of directors' duties; ratification of breaches of director's duties; exercise of management powers; directing directors to take or refrain from taking certain action; approval of loan transactions between directors and company; alteration of the status of a company from public to private; approval of transactions between the company and the shareholder; and winding up the company. Controlling shareholders can extract private benefits of control not only through the exercise of discretionary powers prescribed by the statute, company's constitution or listing rules. They can exercise their powers for their own benefit but at the company's expense through indirect or covert means such as those described above under the category of 'exercise of powers other than by voting'. This chapter has already provided actual evidence of extractions of private benefits of control by controlling shareholders in three of the four countries in common law Asia.

B. Information asymmetry

The second justification for imposing fiduciary duties on directors is to address the problem of information asymmetry.[332] Directors have greater access to, and superior control of, information and resources which could enable them to use the information for their own benefit instead of pursuing the company's interests. Further, directors are in a far better position to know what actions they have taken or not taken, and whether the actions or omissions are in

[332] *Ex parte Lacey* (1802) 31 ER 1228, 1229; *Ex parte James* (1803) 32 ER 385, 345, 349-350; *Ex parte Bennett* (1805) 32 ER 893; Amir N Licht, 'Lord Eldon Redux: Information Asymmetry, Accountability and Fiduciary Loyalty' (2017) 37 *Oxford Journal of Legal Studies* 770.

the company's interests. Thus, directors can provide *ex post* rationalisation for their actions or omissions.

The problem of asymmetric information is exacerbated in the case of controlling shareholders, particularly in the family-owned listed companies in the four countries in Asia. This is because the board and senior management is dominated by the controlling shareholder or his family members. The controlling shareholder or his associates often hold two positions: one as the chair of the board and the other as the CEO, which practically ensures total control of the production, dissemination and use of information. This makes it extremely difficult for minority shareholders to monitor and detect wrongdoing by the controlling shareholder. In SOEs/GLCs, particularly those in Hong Kong, Malaysia and India, information is likely to be controlled by the controlling shareholder, which is the government or a government-owned entity (or its appointees such as the nominee directors) who wield enormous power over the business and operations of the companies. The controlling shareholder is likely to be much more powerful and influential that the directors.

Information asymmetry has been divided into (i) costly information; (ii) unobservable information and (iii) unverifiable information.[333] Costly information relates to the cost that has to be incurred by the company to monitor the behaviour of directors and controlling shareholder as well as the cost that has to be borne by the directors and controller to comply with any monitoring mechanisms (which could include extensive and expensive reporting and disclosure requirements). Unobservable information is concerned with the inability to evaluate the performance of the directors and controlling shareholder and to detect any breach of duties. A significant number of the listed companies in the four countries in Asia are conglomerates with complex pyramidal structures and opaque cross-holding structures. This makes it extremely

[333] Amir N Licht, 'Motivation, Information, Negotiation: Why Fiduciary Accountability Cannot be Negotiable' in Andrew Gold and D Gordon Smith (eds), *Research Handbook on Fiduciary Law* (Edward Elgar 2018).

difficult for minority shareholders (who are generally apathetic and reticent) to know whether and how the directors or the controlling shareholders have exercised their powers and to what ends. Detecting extractions of private benefits of control becomes formidably difficult, if not impossible, unless substantial cost is incurred. Unverifiable information means that although there is information on the misuse or abuse of powers by directors or controlling shareholder, the information may be either inadmissible in court for the purposes of proving breach (perhaps because it is hearsay or anecdotal), the court does not have the expertise to assess the evidence, or the court does not have the information-gathering powers to collate the information.

Thus, controlling shareholders can take advantage of the fact that information is costly, unobservable and/or unverifiable to extract private benefits of control to the detriment of the company. And given that controlling shareholders have access to better or more information, non-controlling shareholders will not be able to fully appreciate the significance or consequence of controlling shareholder who voted for or against certain resolutions (such as those pertaining to approving a major transaction or exercising management powers). This in turn allows the controlling shareholder to extract private benefits of control. Accordingly, if regulating information asymmetry is a well-established basis for imposing fiduciary duties on directors, then what more for controlling shareholders in complex listed companies, particularly the family-owned companies and SOEs in the four countries in Asia.

C. Incomplete contracts

The third and final justification for imposing fiduciary duties on directors rests on the notion of incomplete contracts: it is costly, impracticable and even impossible to list out every conceivable instance of opportunistic behaviour by directors in the form of a written contract between the directors and company and to list out every single circumstance that would constitute a breach and the remedies that are available for each and every breach.[334] Given the intrinsic complexity and unpredictability of factual situations involving conflicts of interest, contracts are necessarily incomplete. The same rationale should also apply to controlling shareholders. It is not any more cost-effective for controlling shareholders to enter into a contract with the company and non-controlling shareholders to specify in advance all the permissible and impermissible transactions, and all the permissible and impermissible uses of information. It is likewise costly and impracticable to list out in advance all the *ex ante* benefits and costs arising from a particular exercise of voting power or influence, or a particular transaction or particular use of information by the controlling shareholder.

To elaborate, controlling shareholders would be in possession of more, and would have better and quicker access to, valuable information than non-controlling shareholders. What makes the company and minority shareholders especially vulnerable is that controlling shareholders could use the information to benefit themselves but at the expense of the company and minority shareholders. Illustration of the different types of information that could be possessed and used by controlling shareholders can be found in the examples given under the section 'Major transactions', 'Existing business relationships with the company', 'Exploitation of corporate opportunities' and 'Investments in competing companies'.

However, it is very difficult and costly to contract over the use of information for three reasons. First, it is difficult to ascertain the value of information until all the relevant information is disclosed. But in the first place, such disclosure would require the parties to the contract to specify in advance which information can and cannot be used and under what

[334] See Jean Tirole, 'Cognition and Incomplete Contracts' (2009) 99 *American Economic Review* 265; Robert H Sitkoff, 'The Economic Structure of Fiduciary Law' (2011) 89 *Boston University Law Review* 1038 (2011) 1040-1041.

circumstances and by what criteria, which is a very difficult and costly exercise. Second, controlling shareholders would be particularly unwilling to disclose private information as it would have significant strategic value. The result is that controlling shareholders would only disclose bits of such information (if at all), and the non-controlling shareholders would be spending much time and resources to extract as much of such information as possible from the controlling shareholders and at the same time trying to determine the value and accuracy of such information. Finally, even if all the relevant information has been disclosed, and even if all the circumstances in which the information can or cannot be used are exhaustively stated in the contract, it would still be prohibitively costly for the company and non-controlling shareholders to monitor every compliance and detect every infringement.

Subjecting controlling shareholders to fiduciary duties should produce two benefits. The first and most obvious one is that it will minimise transaction costs. The second is that to the extent that controlling shareholders would want to use the information for their own benefit, they should be incentivised to seek authorisation from a board (comprising directors who are neither connected to nor are nominees of the controlling shareholders);[335] otherwise they may be in breach of their fiduciary duties. Thus, for instance, should the controlling shareholder wish to exploit a corporate opportunity, he should obtain advance consent from such a board. Or consider another example mentioned above. A shareholder is a controller in two different but competing companies, A and B. If the controlling shareholder would like to use the information that he has of acquired of Company A for the purpose of voting on matters in Company B, being subjected to fiduciary duties should incentivise him to obtain authorisation from Company A. It might be argued however that in those two examples, the parties to the contract could simply add a clause to the contract stating that the controlling shareholder is prohibited from using any information that (a) he has obtained in the course of being a

[335] See Chapter 4.

controller or (b) could benefit him or an entity connected to him. However, it is unlikely that the controlling shareholder would agree to such a blanket prohibition without first knowing what the precise information is, what its actual (as opposed to hypothetical) value is, and whether the benefits from using the information exceed the costs. But the controlling shareholder may agree if the contract lists out in detail and in advance the precise information that can or cannot be used and the precise purposes and circumstances in which it is used. However, as discussed earlier, this is impracticable and costly to all parties. Thus, fiduciary duties solve two problems at one go: reduction of transaction cost, and reduction of extractions of private benefits of control by incentivising the controller to seek advance consent by making specific disclosure of specific use of a specific piece of information, failing which he would likely be in breach of his duties.

To conclude, in this chapter, I first highlighted the significant and substantial powers wielded by shareholders. I then explained the two types of concentrated ownership companies in the four Asian jurisdictions (i.e. families and SOEs) and I showed the persistent and pervasive problems of extractions of private benefits of control in these listed companies. Subsequently, I put forward three key justifications as to why controlling shareholders should be subject to fiduciary duties: (1) the *ex ante* and *ex post* mechanisms for regulating extractions of private benefits of control are deficient; (2) there are conflicts of interest involving controlling shareholders which can lead to extractions of private benefits of control that are not regulated by the current law; and (3) the reasons for subjecting directors to fiduciary duties also apply to controlling shareholders. In the next chapter, I will explain what the contents of these fiduciary duties should be.

DPHIL CHAPTER 4: CONTENTS OF FIDUCIARY DUTIES

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II. Duty to avoid unauthorised conflict of interest and unauthorised receipt of profits

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In the previous chapter (Chapter 3), I explained why fiduciary duties should be imposed on the controlling shareholders of the listed companies in the four Asian common law jurisdictions. The aim of this chapter (Chapter 4) is to critically analyse what the contents of these duties should be, and in Chapter 5, I will examine the circumstances under which the duties should be imposed, who should impose the duties, and how they should be imposed.

I have explained in Chapter 1 why two fiduciary duties are examined in this thesis, namely, the duty to act in good faith in the best interests of the company, and the duty to avoid unauthorised conflicts of interest and unauthorised receipt of profits. There are two key issues in relation to the best interest duty, namely, the meaning of the term the "interests of the company", and whether a subjective test, objective test or a combination of both applies to this duty. The issue in relation to the no-conflict and no-profit rule is how controlling shareholders can obtain authorisation for conflicts of interest. These issues will be examined in this chapter.

With respect to the first issue of the best interest duty, I argue that corporate interest can refer to the long-term value and viability of a company, whose interests are separate and distinct from (although they may overlap with) those of shareholders or stakeholders; corporate interest need not be equated with the interests of shareholders as a whole or those of stakeholders. There is a normative, legal and empirical basis to my argument. Normatively, after summarising the critiques of two conventional theories (i.e. shareholder primacy and stakeholder theory), I draw on three theories, namely, entity maximisation and sustainability theory, company-centred theory, and systems theory to support my argument. Legally, I show that the laws of Singapore, Malaysia and India not only do not require that corporate interest be equated with shareholders' interests, but rather, the former can be preferred over the latter. What is more, Indian law specifically recognises and requires corporate interest to be protected. Hong Kong law however equates the interests of the company with those of shareholders. Empirically, I analyse the corporate purposes of the top 30 listed companies by market capitalisation in the four Asian jurisdictions. A key finding is that a majority of these companies do not have shareholder maximisation as their corporate purposes; rather, a significant percentage of these companies have corporate purposes that prioritise the interests of the company as a distinct and separate commercial entity. Subsequently, I examine the second issue pertaining to the best interest duty. I argue that the best interest duty should consist of a combination of a subjective (i.e. whether the controlling shareholder honestly thinks that he is acting in the company's best interests) and objective test (i.e. courts will not invalidate the controlling shareholder's action unless it is one that no reasonable controller could have come to).

After analysing the duty to act in good faith in the best interests of the company, I examine the no-conflict and no-profit rule. A key issue is that because this rule only prohibits unauthorised conflicts of interest, I argue that subject to appropriate safeguards, the four Asian countries should have an authorisation mechanism that allows the board of directors to authorise conflicts involving the controlling shareholder.

I. Duty to act in good faith in the best interests of the company

A. Interests of the company

There is an indivisible relationship between the separate legal personality rule, corporate purpose and corporate interest. As a result of separate legal personality rule, the company has an identity that is separate and distinct from its shareholders, and legal capacity is given to the company to pursue purposes that are not synonymous with those of its shareholders and other stakeholders. The legal capacity enables companies to create and benefit from legal rights or incur legal liabilities for itself that are independent of the rights and obligations of the shareholders and directors. The rights enjoyed, and obligations borne, by the company are neither derived from, nor are the aggregation of, those of the shareholders.

To state the obvious, a company can sue and be sued, can own assets, and can enter into contracts, all in its own name. Just as shareholders are not liable for the company's debts, the reverse is also true. If the company is an aggregation of its members, then the rights and liabilities of the company will be derived from its members. But this is not the case.[1] The rights (including but not limited to owning property, entering into contracts and commencing legal proceedings) are conferred on the company once it is legally incorporated, irrespective of the rights of its members. Nor are the debts of the company 'derived' from those of its shareholders.

Thus, as a result of separate legal personality, a company is able to define and pursue its own purposes, which are distinct from those of the shareholders or other stakeholders (although they may overlap). Corporate purpose impacts on corporate interest.[2] For example, if a company defines its fundamental or ultimate purpose in terms of financial gain, the company is likely to equate its interest with those of the shareholders, as reflected in the

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[1] Cf The nexus of contract theory views companies 'as legal fictions which serve as a nexus for a set of contracting relationships among individuals': Michael C Jensen and William H Meckling, 'Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure' (1976) *Journal of Financial Economics* 305, 310. For trenchant criticisms, see Michael Klausner, 'The "Corporate Contract" Today' in Jeffrey N Gordon and Wolf-Georg Ringe (eds), *Oxford Handbook of Corporate Law and Governance* (OUP 2018) Ch 4; Marc Moore, 'Private Ordering and Public Policy: The Paradoxical Foundations of Corporate Contractarianism' (2014) 34 *Oxford Journal of Legal Studies* 693; Paddy Ireland, 'Property and Contract in Contemporary Corporate Theory' (2003) *23 Legal Studies* 453.

[2] Big Innovation Center, *The Purpose Company: Interim Report* (May 2016) <http://www.biginnovationcentre.com/media/uploads/pdf/The%20Purposeful%20Company%20Interim%20Report.pdf> accessed 1 December 2018; Big Innovation Center, *The Purposeful Company: The Policy Report* (February 2017) <http://www.biginnovationcentre.com/media/uploads/pdf/TPC_Policy%20Report.pdf> accessed 1 December 2018.

maximisation of share price. But if a company defines its fundamental or ultimate purpose in terms of being the best provider of certain goods or services, or a leading contributor of certain benefits or welfare to the society in which it operates, its corporate interest is not likely to be reducible to, nor synonymous with, the interests of shareholders or any specific stakeholder, as will be shown in the section 'Empirical' below.

However, what constitutes the interests of the company is not merely a factual or empirical matter that can discerned from what the company says or does. This is because there is also a legal understanding of corporate interest in view of the statutory provisions and case law, which will be examined under the section 'Legal'. In other words, unless the law stipulates what corporate purpose is, it remains a factual question, as demonstrated by what the company says and does. But because there is a corpus of law on corporate interest, the latter is a legal question, in addition to being a factual one (as discerned from the company's avowed corporate purpose).

In what follows, I will argue that there is legal and empirical support for the claim that corporate interest, in the legal and empirical sense, can be distinct from that of the shareholders and other stakeholders. But it might be objected that because the company, an artificial entity, can only act through its agents and as the company comprises different constituencies, it does not have purposes and interests that are distinct and separate from those of its agents and constituencies.

This objection does not adequately account for the reality of complex organisations with multiple constituencies who have competing and conflicting interests. Similar to other complex, social organisations (such as universities), companies can have institutional or collective purposes that can neither be equated with, nor reduced to, those of their constituents, the latter of whom are often heterogenous, and thus have diverse, competing and conflicting aims and interests within and among themselves.[3] This is particularly true in complex entities like listed companies that have multiple subsidiaries and different types of constituencies (shareholders, employees, creditors, suppliers and customers). Further, even within a specific category of constituencies, such as shareholders, there are competing and even opposing goals and interests such as those between controlling and minority shareholders, long- and short-term shareholders, and passive and activist shareholders.

In other words, the fact that individuals or different groups of individuals are involved in the formation, management and control of the company or have contributed to the company (in the form of money, assets, labour, skills, etc) – the fact that individuals come together to

[3] For example, Hansmann shows that while "investor-owned firms" are common and well-established, they are not the only types of firms. There are the employee-owned firms (such as law firms and accounting firms), farmer-owned producer cooperatives, consumer-owned utility firms, and mutual companies owned by their policyholders. Thus, one may draw on his work to support my claim that it is incorrect to necessarily equate the interests of the firm with those of shareholders. See Henry Hansmann, *The Ownership of Enterprise* (Harvard University Press 1996). But it may be objected that Hansmann's analysis may undermine my claim in three ways. First, while the interests of the firm need not be equated with those of shareholders, they have to be equated with the owners, whether they be the employees, consumers or policyholders, and not with the corporate entity itself. The rebuttal is that my claim is not undermined because the law governing the particular types of business organisation, such as partnership, which applies to "employee-owned firms" such as law firms, equates the interests of the partnership with those of its employees. In a partnership, partners own the assets of the partnership, and they owe fiduciary duties to each other for they act as principals and agents of each other. By contrast, under company law, shareholders do not own the company's assets, they do owe fiduciary duties to each other, and directors do not owe fiduciary duties to shareholders. Second, because Hansmann provides persuasive reasons (in Chapter 4) as to why shareholders should be given control over the company (such as the right to appoint and dismiss directors and the right to approve mergers and dissolution of the company), this in turn implicitly supports the shareholder primacy theory. I have two rebuttals here: (1) it is not my claim that shareholders should not be given control rights; nor is the goal of my thesis to justify why controlling shareholders should be given control rights. Rather, my aim is to show why fiduciary duties should be imposed on controlling shareholders. In other words, I seek to show how controlling shareholders should exercise their control rights. (2) It is important to note that while Hansmann is robust in his defence of why shareholders should be the residual claimants (see pg 53-56), his defence of why shareholders should have control rights is equivocal (see pg 57-64). He acknowledges that shareholders (in dispersed ownership jurisdictions) are not good monitors of managers and they face collective action problem. The third and final way in which Hansmann's analysis may be said to undermine my claim is that he endorses the view that the firm is a nexus of contract, which is at odds with the real entity view that I accept. My response is this. It is important to understand what Hansmann exactly says. He begins by asserting (at pg 18) that "… it helps to view the firm ... as a nexus of contracts". He then says (at pg 18-19) that "a firm is in essence the common signatory of a group of contracts… Indeed, one of the most important functions of organizational law is to permit the creation of a juridical person-a single legal entity-that can serve as signatory to contracts." This shows that he accepts the importance of the firm as a separate legal entity. It is arguably more correct to say that what underpins Hansmann's theory is the real entity theory, rather than the nexus of contract theory. After all, his key aim is to explain why those who enter into contracts with the firm – shareholders who provide capital (in investor-owned firms), employees who provide services (in employee-owned firms), consumers who purchase the firm's products and services (in consumer-owned firms) – are given control rights. His analysis assumes and relies on the firm as a separate legal entity which is capable of entering into contracts with these different parties.

use or participate in the corporate entity to achieve certain goals for themselves – does not tell us anything conclusive about the nature, purposes and interests of the institutional enterprise or the effects that are sought to be achieved by this collective endeavour.[4] After all, the company is more than the aggregation of its parts. The different constituencies within the company come and go for they have finite existence and interests. But this is not the case for the company which has perpetual existence (unless it is wound up).[5]

Further, a fundamental and serious objection to the view that the interests of the company should be equated with those of shareholders is its implicit reliance on, and endorsement of, this assumption: shareholder primacy or shareholder value maximisation theory is correct and other rival theories (such as the stakeholder approach) are wrong. Intrinsic to the claim that the interests of the company should be equated with those of shareholders is a bias towards shareholder primacy theory. It is critical that proponents of this view explicitly acknowledge and defend this assumption. Unless and until they discharge this burden, there is no *a priori* reason why we should equate the interests of the company with those of shareholders. I will show below that the reasons in support of this theory are questionable.

Finally, I demonstrate that there is support for the view that the interests of the company need not be (from a normative perspective) and are not (from a legal and empirical perspective) equated with those of the shareholders (or other constituencies). Rather, there is normative, legal and empirical recognition of corporate interest as distinct and separate from the interests of its constituencies, which supports my argument that acting in the best interests of company can mean protecting and promoting the long-term value and viability of the company.

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[4] Lyman Johnson, 'Relating Fiduciary Duties to Corporate Personhood and Corporate Purpose' in D Gordon Smith and Andrew Gold (eds), *Research Handbook on Fiduciary Law* (Edward Elgar 2018) (forthcoming); Eric W Orts, *Business Persons: A Legal Theory of the Firm* (OUP 2013).

[5] Lynn Stout, 'The Corporation as Time Machine: Intergenerational Equity, Intergenerational Efficiency, and the Corporate Form' (2015) 38 *Seattle University Law Review* 685.

Before proceeding further, I should make two clarifications. First despite the flaws in the shareholder primacy and stakeholder value theories, it is not my claim that my argument – corporate interest as the long-term value and viability of the company – should supersede these two theories. Rather, my intention is to present another approach, one that to my mind has normative, legal and empirical basis, for the purpose of interpreting the best interest duty to which controlling shareholders should be subject. Second, subjecting controlling shareholders to the duty to act in good faith in the company's best interests will not result in courts taking control of the company's business decision whenever there is a law suit against the controllers for breach of the best interest duty. As I will show in Part I(B) below, as long as the controlling shareholders honestly believed that the decision that they have made was in the company's best interests, courts will not and should not invalidate the decision unless it is one that no reasonable controller could have ever come to. The standard is irrationality, not unreasonableness.

1. Normative

There is voluminous literature analysing shareholder value maximisation theory (including its modern incarnation the enlightened shareholder value) and stakeholder value theory. But far less has been written about promoting and protecting the long-term value and viability of the corporate entity, which is the view that will be endorsed for the purpose of determining what the company's interests are in relation to the fiduciary duty of controlling shareholders to act in the company's interests.

In brief, the reasons for adopting a shareholder value maximisation/enlightened shareholder value approach are that (1) shareholder are the owners[6]; (2) they are the principals[7]; (3) they are the residual claimants[8]; and (4) it provides a clear and quantifiable criterion for fiduciaries to manage the affairs of the company, thereby constraining them from pursuing their own interests.[9]

The rebuttal to the first reason is that because of the separate legal personality doctrine, shareholders only own shares and not the company. Regarding the second reason, if it were true that shareholders were the principals and directors their agents, then directors would owe them fiduciary duties. But this is false as directors only owe fiduciary duties to the company and only the latter can enforce them against the directors. With respect to the third reason, shareholders are the residual claimants only when a company is insolvent or, although solvent, is voluntarily wound up. Shareholders are not legally entitled to dividends unless and until the board declares them but it is not legally obligated to do so. Whether a solvent, profit-generating company should adopt shareholder value maximisation depends not on whether shareholders are the residual claimants when it is insolvent. Rather, it depends on whether maximising shareholder value benefits the company (and therefore society) over time. But it has not, as shown in the decline of share price, shorter life span of companies, reduction in R&D investments, excessive risk-taking and short-termism.[10] Even the enlightened shareholder

[6] Milton Friedman, 'The Social Responsibility of Business is to Increase its Profits' *New York Times Magazine* (13 Sep 1970) 124.

[7] Jensen (n 1); Reiner Kraakman and others, *The Anatomy of Corporate Law* (2nd edn, OUP 2009) 36.

[8] Frank H Easterbrook and Daniel R Fischel, *The Economic Structure of Corporate Law* (Harvard University Press, 1991) 36-7; Eugene F Fama and Michael C Jensen, 'Organizational Forms and Investment Decisions' (1985) 14 *Journal of Financial Economics* 101, 102-3.

[9] Michael C Jensen, 'Value Maximisation, Stakeholder Theory and the Corporate Objective Function' (2002) 12 *Business Ethics Quarterly* 235, 238.

[10] See eg, Lynn Stout, *The Shareholder Value Myth: How Putting Shareholders First Harms Investors, Corporations, and the Public* (Berrett-Koehler Publishers 2012) Ch 4; European Commission Green Paper, *Corporate Governance in Financial Institutions and Remuneration Policies* COM (2010) 284 final, 8; European

value approach reflected in s 172 of the UK Companies Act 2006 has 'actually reinforced in practice a short-term shareholder value maximisation version of shareholder primacy that is detrimental to society.'[11] In any event, stakeholders who make specific investments in the company (such as employees who acquire and contribute uniquely valuable expertise to the company) and whose interests cannot always be protected using contracts should also acquire residual interest in the company.[12] The rebuttal to the fourth reason is that it is doubtful that long-term shareholder value can provide a clear and determinate metric for fiduciaries to discharge the duties that they owe to the company.[13] While short-term shareholder value can do that, it has engendered material and adverse consequences on companies and societies.[14] Given that companies are entities that are capable of lasting indefinitely, there is significant and substantial uncertainty with respect to their future business operations and financial conditions. As a result, there may be difficulties with providing an objective quantification of long-term shareholder value, especially because there are doubts as to whether the share price

Commission Green Paper, *The EU Corporate Governance Framework* COM (2011) 164 final, 11; John Kay, *The Kay Review of UK Equity Markets and Long-term Decision-Making, Final Report* (London: Department of Business, Innovation and Skills, 2012) paras 1.1-1.29; William Lazonick, 'Profits Without Prosperity' (2014) *Harvard Business Review* < https://hbr.org/2014/09/profits-without-prosperity> accessed 1 December 2018. Cf Mark J Roe, 'Stock Market Short-Termism's Impact' (May 25, 2018) <https://ssrn.com/abstract=3171090> accessed 1 December 2018. A key evidence cited by Roe to refute the point that short-termism has resulted in reduction of R&D is that R&D has overall increased, led by the top 5 tech companies in the US (Apple, Amazon, Microsoft, Alphabet (Google) and Facebook) which are also the top 5 listed companies in the US. But a review of the annual reports, mission statements and other publicly available documents shows that these top 5 tech companies do not adopt the maximisation of share price as the sole or predominant corporate purpose. Rather, they have defined their corporate purpose in terms of being the best customer centric company in the world (Amazon), and delivering the best products and services to consumers and community in their respective domains (Apple, Google and Microsoft).

[11] Eilis Ferran, 'Corporate Mobility and Company Law' (2016) 79 *Modern Law Review* 813, 836.

[12] Margaret Blair, *Ownership and Control: Rethinking Corporate Governance for the Twenty-First Century* (Brookings Institute 1995) 231.

[13] Tamara Belinfanti and Lynn Stout, 'Contested Visions: The Value of Systems Theory for Corporate Law' (2018) 166 *University of Pennsylvania Law Review* 579, 596-598.

[14] (n 10).

is capable of reflecting the long-term, fundamental value of the company.[15] Further, uncertainty exacerbates the difficulty of valuing these companies.[16]

The reasons to adopt the stakeholder approach are that (1) stakeholders, particularly employees, cannot adequately protect themselves through contracts when they make firm-specific investments; (2) stakeholders such as employees, customers, suppliers and the community could be as materially and adversely affected by the company's decisions as shareholders or even more so; (3) stakeholders should not be treated as a means to advance the interests of shareholders but as an end in themselves on the basis of fairness and equality; and (4) the promotion and protection of stakeholders' interests are necessary for the long-term sustainability and prosperity of the company.[17]

The main criticisms of the stakeholder approach are that (1) non-shareholders do not have enforcement powers; (2) it is difficult to weigh and balance so many competing and conflicting interests and even if practicable, the criteria for doing so are unclear; (3) it gives significant discretionary powers to fiduciaries and there is therefore room for them to act opportunistically; and (4) stakeholders' concerns should be addressed through regulations other than company law, the latter of which should be primarily concerned with the regulation of the internal constituencies of the company particularly the relationships among shareholders and those among shareholders and directors.[18]

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[15] For a trenchant analysis, see William W Bratton and Michael L Wachter, 'The Case Against Shareholder Empowerment' in William W Bratton and Joseph A McCahery (eds), *Institutional Investor Activism: Hedge Funds and Private Equity, Economics and Regulation* (OUP 2015) 707-759

[16] Valuation methods include discounted cash flow, dividend discount, comparable company analysis etc: see eg, Simon Z Benninga and Oded H Sarig, *Corporate Finance: A Valuation Approach* (McGraw-Hill Higher Education 1997).

[17] See eg, Gavin Kelly and John Parkinson, 'The Conceptual Foundations of the Company: A Pluralist Approach' in John Parkinson and others (eds), *The Political Economy of the Company* (Hart 2001) 123-129.

[18] See eg, John Argenti, 'Stakeholders: The Case Against' (1997) 30 *Long Range Planning* 442; Elaine Sternberg, *Stakeholding: Betraying the Corporation's Objectives* (London Social Affairs Unit Research Paper No 27, 1998). These criticisms can be addressed by showing how the present company law system can be

Other than shareholder primacy and stakeholder theory, another approach focuses on the long-term well-being of the company as a real entity that is separate and distinct from shareholders and other stakeholders (although its well-being is dependent on the contributions of these stakeholders). This approach gives effect to the fundamental rule of separate legal personality and to another fundamental feature of the company – its capacity to last forever. The corollary is that the purposes and interests of the company are distinct from those of its stakeholders, and given its perpetual life, it has to be managed on a long-term basis with a view to the future. It has been said that companies 'were devices to ensure long-term commitment to shared goals and risks, with reciprocal obligation on those who engaged with them.'[19] And because companies have a pervasive and profound impact not only on their stakeholders, but also on the general economy and broader society, companies have to be managed with a view to the consequences that they bring about.

Scholars have given theoretical grounding to this approach. Keay comes up with the entity maximisation and sustainability model (EMS)[20]. Bower and Paine develop a 'company-centered' model that has 'at its core the health of the enterprise rather than near-term returns to its shareholders.'[21] Stout propounds the corporation as a system model under which the company can and should pursue long-term projects that benefit future generations.[22] All three

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reformed to operationalise stakeholder theory: see Iris Chiu, 'Operationalising a Stakeholder Conception in Company Law' (2016) 10 *Law and Financial Markets Review* 173. In addition to her trenchant criticisms of the shareholder maximisation theory and the enlightened shareholder model, Chiu rebuts the criticisms of stakeholder theory by demonstrating why and how companies should enter into stakeholder covenants with key stakeholders backed up by directors' duty to comply with such covenants, as well as how these covenants can be enforced.

[19] Big Innovation Center, *The Purpose Company: Interim Report* (May 2016) 7 <http://www.biginnovationcentre.com/media/uploads/pdf/The%20Purposeful%20Company%20Interim%20Report.pdf> accessed 1 December 2018.

[20] Andrew Keay, 'Ascertaining the Corporate Objective: An Entity Maximisation and Sustainability Model' (2008) 71 *Modern Law Review* 663.

[21] Joseph L Bower and Lynn S Paine, 'The Error at the Heart of the Corporate Leadership' (2017) *Harvard Business Review* < https://hbr.org/2017/05/managing-for-the-long-term> accessed 1 December 2018.

[22] Stout (n 5).

models are in turn premised on the real entity theory (as opposed to the fiction theory which views the company as a creation of the state or the aggregate theory which treats the company as merely the sum of its shareholders).[23] I argue that the writings of these scholars support my position that the term "the company's interests" in relation to the fiduciary duty of the controlling shareholders to act in the company's interests refers to the long-term value and viability of the company.

i. Entity maximisation and sustainability model

Keay's EMS model comprises two limbs. The first focuses on enhancing the company's wealth (which is different from maximising shareholder value) and the second on sustaining the company as a going concern. Regarding the first, the overall long-term market value of the company as a whole has to be enhanced. EMS does not ask which stakeholder's interest should be protected and how; rather it asks how we should protect the long-term interests of the company. To achieve the goal of protecting corporate interest, shareholders' dividends may have to be increased, employee compensation and benefits may have to be increased, the company's reputation may have to be enhanced, creditors' risk may have to be reduced, investments in R&D may have to be increased, and excessively risky investments have to be avoided.[24] Achieving the goal of corporate interest is context driven. The context can refer to the company's values and priorities as well as industry and market conditions. For example, promoting the long-term interest of a company has a different meaning for a company whose

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[23] From an historical and legal perspective, the real entity is the most persuasive theory as compared to the fiction and aggregate theory: Reuven S Avi-Yonah, 'The Four Transformations of the Corporate Form' in Barnali Choudhury and Martin Petrin (eds), *Understanding the Company: Corporate Governance and Theory* (CUP 2017) 17-36.

[24] Keay (n 20) 685.

mission is to deliver public services such as utilities as compared to an investment-holding company with few or no employees and creditors. Further, at certain times, promoting the long-term corporate interest may require the company to use its cash to increase its expenditure in R&D instead of issuing dividends. At other times, the company may reject a potentially profitable project in order to protect its reputation such as not setting up factories in third world countries where there is evidence of exploitation of workers and other human rights abuses.[25] To be clear, EMS neither assumes nor implies that a company's financial performance is secondary or unimportant. Rather, it rejects the notion that performance of the company is to be equated with the maximisation of share price. For example, if a company has not been profitable or is even making losses, the company may decide to close down a factory, or temporarily freeze bonuses to employees. This will hurt the interests of employees but can be justified on the basis that it is necessary to protect the company's long-term interests, which certainly entail financial performance.

Keay anticipates and rebuts the criticism that maximising the corporate entity's interests requires balancing and weighing competing and conflicting interests of different stakeholders, which is the same objection levelled against the stakeholder approach.[26] He argues that whereas balancing the interests of different stakeholders is an end in stakeholder theory, balancing under EMS is a means to achieve the single overall goal of enhancing the long-term interests of the company.[27]

Ultimately, he argues that EMS has the ability to engender trust and loyalty among employees, customers, suppliers who make firm-specific investments. This is because they know that because the focus is on the long-term interests of the company and not on the

[25] Ibid 685.

[26] Ibid 687.

[27] Ibid 687.

maximisation of shareholder value, the latter of which would often necessitate sacrificing the interests of non-shareholders if it does not lead to the maximisation of share price.[28]

Regarding the second limb of EMS, i.e. sustainability, while recognising that sustainability is used in different senses, Keay uses it to mean specifically financial sustainability, that is, 'both the survival of the company, namely the company does not fall into an insolvent position from which it cannot escape, and the continuing development of the financial strength of the company.'[29] In short, the first limb refers to growth, and the second, survival. Companies have to promote their long-term interests while ensuring that they survive in the short-term by taking into account financial stability. Keay underscored the importance of corporate survivability by mentioning how one wrong decision could render the company insolvent.[30]

The difference between EMS and shareholder value maximisation lies not only in the purpose but also in the course of action to achieve the purpose. For example, a company may decide to lay off workers or not invest in the R&D in order to use the cash to issue special dividends to shareholders. However, under EMS, it is unlikely that companies will take such a course of action because it will not only hurt employees' morale but more importantly, jeopardise the company's long-term growth. The differences between EMS and stakeholder theory are twofold.[31] First, under stakeholder theory, the company may decide to use the cash it has to increase employees' salaries instead of paying more dividends to shareholders. In contrast, under EMS, the company may do so but for a different reason: the company may take

[28] Ibid 688-689.

[29] Ibid 691.

[30] He gives the example of the Barings Bank trader whose fatal trading decision caused the bank to collapse (at 692).

[31] Ibid 696.

the view that boosting employee morale is critical for the long-term interest of the company in light of a persistent problem of low retention rates for staff. Second, under EMS, directors are agents of the company whereas under stakeholder theory, directors are agents of the stakeholders.

In sum, EMS - augmenting the wealth of the corporate entity and ensuring the financial sustenance of the company - provides normative support for the position advanced here, namely, to act in the best interests of the company is to protect and promote the long-term value and viability of the company.

ii. Company-centered model

Other proponents who take the view that the company is a real entity and whose distinct interests should be protected and promoted are Bower and Paine from Harvard Business School.[32] They emphasise the features of the company (its separate legal personality and its capacity to last forever), the varied purposes of companies, the means through which companies have been used as vehicles for large-scale projects, as well as the impact companies have had and continue to have on the market and society. They debunk the agency theory and articulate eight propositions for their 'company-centered model' which offer 'a radically different and… more realistic foundation for corporate governance and shareholder engagement.'[33]

First, the effective functioning of companies – setting and implementing strategies, retaining and attracting talents, and allocating scarce resources in light of competing demands

[32] Bower (n 21).

[33] Ibid.

– depend more on the expertise, experience, motivation and character of management than on aligning executive compensation with shareholder returns.

Second, in light of rapidly changing and unpredictable technological and industry standards, the success of companies depends more on whether they can innovate and are flexible than on setting well-defined goals and providing incentives and rewards for individuals to achieve those goals.

Third, given that companies perform multiple functions that impact on different interests such as creating jobs, spurring innovations, and providing goods and services, corporate purpose cannot be reduced to one single overriding objective such as shareholder value maximisation.

Fourth, in view of the diversity of purposes that companies have, they will and should have different strategies for achieving them, and thus, having one single metric to evaluate the performance of companies such as total shareholder returns is not appropriate.

Fifth, in order for companies to thrive in the long-term, they have to create value for different constituencies (customers must want their products and services, employees must want to work for them, creditors must want to lend them money, shareholders must want to invest in them, and the communities in which they operate must want their presence) and where conflict arises, determine which trade-offs are necessary; thus, requiring companies to act solely or primarily for the benefit of shareholders (as required by the shareholder value maximisation/enlightened shareholder approach) oversimplifies the difficulties of managing the companies.

Sixth, shareholder value maximisation theory/enlightened shareholder approach has nothing valuable to say about ethical standards that go beyond not engaging in fraud or collusion to which companies have to adhere in order to sustain trust among its constituencies.

Seventh, as the long-term interests of companies are also tied to the interests of the communities in which they operate, companies have to be concerned with negative externalities caused by their activities and have to undertake corporate social responsibilities, important issues of which the typical shareholder value maximisation theory have nothing much to say and to which the enlightened shareholder value approach pays lip service.

Finally, the interests of the company are distinct from those of shareholders and the latter do not have homogenous interests.

Bower and Paine assert that '[t]hese propositions underscore the need for an approach to governance that takes the corporation seriously as an institution in society and centers on the sustained performance of the enterprise.'[34] Their theory lends support to my position that to act in the company's interests is to promote and protect the long-term value and viability of the company.

iii. The company as a system model

Stout's starting point is the two fundamental features of the company – separate legal personality and perpetual life – which allow companies to pursue large-scale, long-term projects under complex and uncertain conditions.[35] A corollary of separate legal personality is that companies can 'lock-in' their assets and shield them from shareholders and the latter's creditors. This in turn allows non-shareholders (such as employees, customers, suppliers and creditors) to make 'specific investments' in the company, such as tangible or intangible assets, skills, time or resources. These investments are often required for large scale, long-term and

[34] Ibid.

[35] Stout (n 5).

uncertain projects (such as building large infrastructure including railways, airports, aircrafts, as well as developing new technologies such as artificial intelligence). If shareholders can withdraw the cash they have invested or simply demand that the board pays them dividends, in other words if assets are not 'locked in', the projects may be stalled or terminated and the non-shareholders may be held hostage to the actions of the shareholder and would thus be disinclined to make those specific investments in the first place.

Regarding the second feature, perpetual life, because the company can, in law, last forever (unless it becomes insolvent or is struck off from the company register), the company can continue to develop projects for a very long time into the future, although the shareholders and stakeholders who make the specific investments come and go. Thus, companies can have profound and far-reaching impact on the well-being of not only on its present constituencies, but also future ones.

Thus, in understanding what the interests of the company are, we have to take into account the future interests of the company. But it is impracticable to predict how long or how well the company will last into the future beyond a certain time frame. However, given that the company can only achieve its purposes if it survives and if it lasts for at least a certain period of time, Stout argues that 'the most fundamental measure of corporate performance may be, first and foremost, continued corporate functioning.'[36] This is similar to the second limb of Keay's EMS which emphasises on the survivability of the company.

[36] Lynn Stout, 'The Corporation and the Question of Time' in Barnali Choudhury and Martin Petrin, *Understanding the Company: Corporate Governance and Theory* (CUP 2017) 303.

Stout then introduces the idea of viewing companies as a system, deriving three lessons from systems theory.[37] First, systems theory defines a 'system' as consisting of independent but connected parts. The system is made up of but is not reduced to, or synonymous with, its parts. Each of these parts come together to achieve a purpose. Applying this insight to the company, the company consists of, but is not reduced to, different constituencies (the employees, suppliers, creditors, customers and shareholders) and different assets and liabilities. Nor can the function or purpose of the company be equated with any particular constituency. Second, systems are meant to operate over certain periods of time, sometimes indefinitely. Thus, a company is usually intended to create jobs, make profit, and produce goods and services, over long periods of time. Third and finally, just as a system will only work if its parts are working well (think of washing machine or coffee machine), so will the company: provided that the different stakeholders are contributing effectively and efficiently to the company, it can produce goods and services, pay taxes, create jobs, and make contributions to the community.

Subsequently, Stout argues that to evaluate the success of the company as a system, one cannot rely on one single metric, be it total shareholder returns or accounting profits, or even employee satisfaction.[38] Rather, a multi-pronged metric that gives effect to the sustainable well-being of the different parts of the system, i.e. the company, is needed. This means that there has to be adequate investments in R&D, employees must be reasonably satisfied, creditors must be prepared to lend at a reasonable cost, and shareholders should be paid appropriate dividends. Crucially, applying and satisfying these metrics are not ends in themselves, contrary to the stakeholder theory or the shareholder value maximisation/enlightened shareholder theory

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[37] Ibid 304-307. See also Belinfanti (n 13) 598-618. Systems theory is a design and assessment methodology used in many disciplines such as computer science (systems analysis), engineering (cybernetics) and management science (operations analysis).

[38] Ibid 309-310.

(the latter of which focuses solely on benefitting the shareholders). Rather, they are means to enable the company to operate on a long-term, possibly indefinite, basis that is sustainable.

iv. Lessons

Lessons can be drawn from Keay's EMS, Bower and Paine's company-centered model and Stout's company as a system model for the purpose of understanding what it can mean for controlling shareholders to fulfil their duty to act in good faith in the best interests of the company, i.e. to protect and promote the long-term value and viability of the company. To begin with, acting in the long-term interests of the company need no longer be measured solely by total shareholder returns, i.e. necessarily equating the interests of the company with those of shareholders. Rather, in determining whether a decision will promote the long-term interests of the company, controlling shareholders should, if the circumstances render it appropriate, take into account and promote intellectual capital (R&D investments, intellectual property), human capital (employees and suppliers), social capital (customers and the community), and natural capital (future generations and environment).[39] This also finds ample empirical support in the avowed purposes of the companies in the common law jurisdictions of Asia, as I will show below under the section 'Empirical': those companies that have defined their purpose in terms of the entity itself and not shareholder primacy or stakeholder value, have explicitly recognised the importance of attending to non-financial capital in order to achieve the corporate objective.

[39] Colin Mayer, 'Who's Responsible for an Irresponsible Business: An Assessment' (2017) 33 *Oxford Review of Economic Policy* 157, 163.

Crucially, there should be strong incentives for controlling shareholders to attend to non-financial capital (i.e. intellectual, human, social and natural) when they exercise their powers because of the evidence of a strong correlation between these non-financial capital and superior stock returns. For example, there is research demonstrating that high employee satisfaction such as companies listed in the '100 Best Companies to Work For in America' produced stock returns that surpassed those of their peers by 2.3% to 3.8% per year over the period 1984 to 2011.[40] Another study demonstrates that companies who are among the top 20% of the American Customer Satisfaction Index performed better than the Dow Jones Industrial Average by 93%, the S&P 500 by 201% and NASDAQ by 335% over the period 1997 to 2003.[41] Another study finds that increases in corporate social responsibility led to a reduction in cost of equity capital over the period 1992-2007.[42] More recently, it has been demonstrated that companies that engage in more corporate social responsibility suffer less from agency problems (such as excess cash, misalignment between managerial pay and corporate performance and expropriation of minority shareholders) and that higher corporate social responsibility is associated with stronger legal protection for minority shareholders.[43]

To clarify, intellectual capital, human capital, social capital and natural capital may not all be relevant to a particular decision and even if relevant, it may not be appropriate to give equal weight to all of them. Some considerations have to be prioritised and trade-offs may be necessary in the short-term in order to protect the company's long-term interests. For example,

[40] Alex Edmans, 'Does the Stock Market Fully Value Intangibles? Employee Satisfaction and Equity Prices' (2011) 101 *Journal of Financial Economics* 621; Alex Edmans, 'The Link between Job Satisfaction and Firm Value, with Implications for Corporate Social Responsibility' (2012) 26 *Academy of Management Perspectives* 1.

[41] Claes Fornell and others, 'Customer Satisfaction and Stock Prices: High Returns, Low Risk' (2006) 70 *Journal of Marketing* 3.

[42] Claes Fornell and others, 'Does Corporate Social Responsibility Affect the Cost of Capital?' (2011) 35 *Journal of Banking & Finance* 2388.

[43] Allen Ferrell and others, 'Socially Responsible Firms' (2016) *122 Journal of Financial Economics* 585.

in deciding whether to vote for or against a major transaction under the listing rules (one that is defined as exceeding 20% or 25% of the value of the company), such as a disposal of assets, what constitute the company's best interests have to be interpreted in light of the company's purpose and the particular circumstances facing the company. If the company is in serious financial difficulty or in dire need of financing, financial capital would and should figure prominently in the decision-making process of the controlling shareholder as to whether the loss-making assets should be disposed of; considerations related to non-financial capital say, natural capital, is unlikely to play a critical or decisive role, unless it impacts on the purpose of the company.

To be clear, the fiduciary duty to act in good faith in the best interests of the company does not bar controlling shareholders from considering their self-interest when they exercise their powers, provided that they prioritise the interests of the company above theirs and that they honestly think that they are acting in the company's interests. For example, controlling shareholders would not be in breach of their duty if they exert influence on the directors to spinoff a loss-making subsidiary that has had no growth for years (although the downside is that those employed by the subsidiary would have to be let go). They put pressure on the board to take such an action because they are of the view that the spinoff would make the company substantially more profitable, and shareholders could ultimately benefit from it in the form of higher dividends. However, they may be in breach of their duty if they pressurise directors to engage in share buybacks, if the value exceeds the company's operating profit or if no consideration is brought to bear as to whether the value of the buybacks would exceed the long-term returns of investing in the future growth of the company.[44] Similarly, they may be in

[44] William Watts, 'BlackRock Warns CEOs Against Buybacks That Only Provide Fleeting Gains' *Market Watch* (24 Jan 2017) <http://www.marketwatch.com/story/blackrock-warns-ceos-against-buybacks-that-only-provide-fleeting-gains-2017-01-24> accessed 1 December 2018; Robert Ayres, 'The Economic Consequences of Shareholder Value Maximisation' (28 March 2017) <https://knowledge.insead.edu/blog/insead-blog/the-economic-consequences-of-shareholder-value-maximisation-5646#4v0c2eecOW0gGEsU.99> accessed 1 December 2018.

breach of their duty if they threaten to or actually dismiss the directors who refuse to issue them with substantial dividends.[45]

Having analysed corporate interest from a normative perspective, the following section examines it from a legal perspective.

2. Legal[46]

I make the following points in this section: (1) Singapore and Malaysian law recognises that the interests of the company are distinct from those of shareholders, and that corporate interest can be prioritised over shareholders' interests depending on the context; (2) Indian law specifically requires the interests of the company as a separate and distinct entity to be protected, in addition to the interests of the shareholders, employees and community; (3) although Hong Kong law is similar to English common law and equates the interests of the company with those of shareholders as a whole, Hong Kong courts should consider adopting the Singapore and Malaysian position; (4) Singapore, Malaysian and Indian law lends support to my position that the notion of the interests of the company — in relation to the duty of controlling shareholders to act in good faith in the best interests of the company — can mean the promotion and protection of the interests of the corporate entity, i.e. the long-term value and viability of the company, which are not necessarily synonymous with or reducible to any shareholder or stakeholder's interests; and (5) Singapore, Malaysian and Indian law, which recognises the

[45] Lynn Stout, 'The Toxic Side Effects of Shareholder Primacy' (2013) 161 *University of Pennsylvania Law Review* 2003.

[46] This section does not deal with the question of whether and how the law recognises the interests of the group company.

protection of the distinctiveness of corporate interest but without specifying what such interest entails, can be elucidated using the normative theories examined earlier.

To begin, under English common law, courts have equated the interests of a company with those of the shareholders as a whole, that is, the present and future shareholders[47], except for insolvent or near-insolvent companies (where the interests of creditors have to be taken into account[48]). This common law principle has been largely codified in s 172(1) of the UK Companies Act 2006 under which directors are required to promote the success of the company 'for the benefit of its members as a whole'. Although the statutory provision requires directors to have regard to the interests of stakeholders (such as employees, creditors, suppliers, customers, the community and even environment), directors have to do so in order to benefit the shareholders. This is the enlightened shareholder value approach. Having regard to the interests of these stakeholders is merely a means to achieve the ends of benefitting the members as a whole. In short, the obligation to act for the shareholders' benefit constrains whether and the extent to which directors can take into account the interests of other stakeholders. However, a key problem is that not only has the overall impact of the enlightened shareholder value approach underlying s 172(1) been negligible, but this provision has also resulted in a perverse consequence as there is evidence that directors have regarded it as a duty to maximise current share price.[49]

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[47] It might be argued that although English common law equates corporate interest with shareholders' interests, directors are not precluded from considering the interests of other stakeholders because directors are likely or ought to do so when they act in the interests of future shareholders. But this objection does not detract from the fact that under English common law, corporate interests is equated with shareholder's interests and consequently, directors have to act solely for their benefit. Any consideration of other stakeholders' interests is subordinated to the central and overriding duty to act in the shareholders' interests. Any benefit to stakeholders is merely incidental. Any regard for these interests is but a means to promote and protect shareholders' interests.

[48] *West Mercia Safetywear v Dodd* [1988] BCLC 250, 252-253; *Brady v Brady* [1988] BCLC 20 [40g]–[41c].

[49] Kay (n 10) 17; Ferran (n 11) 836.

An important issue is whether the courts in the common law jurisdictions in Asia have followed or departed from the English common law and statutory position. None of the four countries has adopted s 172. In relation to the English common law, the case law and the statutory provisions in Singapore and India not only do not mandate the sole or predominant pursuit of shareholders' interests, but instead require the interests of the solvent company as a separate and commercial entity to be given effect to and the interests of non-shareholders to be considered and even protected. Although there are cases in Malaysia that have endorsed the English common law position, recent case law has recognised that the company's best interests refer to different things depending on the contexts. Hong Kong's position however mirrors that of the English common law.

i. Singapore

Case law in Singapore has distinguished the company's interests as a distinct commercial entity and shareholders' interests, and held that where there is a conflict between these two types of interests, the interests of the company can be preferred over those of shareholders.[50] An example of the latter is when directors decided to plough profits back into the company and not pay them as dividends or bonuses.[51] The directors will not be in breach of their duties when they prefer the interests of the company as a commercial entity over those of shareholders.[52] The implications of the court's reasoning are significant. The view that

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[50] *Raffles Town Club Pte Ltd v Lim Eng Hock Peter* [2010] SGHC 163 [162].

[51] Ibid.

[52] Hans Tjio and others, *Corporate Law* (Singapore: Academy Publishing 2016) 363 (citing *Mutual Life Assurance Co of New York v Rank Organisation Ltd* [1985] BCLC 11, 21; *Re RSB Holdings Ltd (No 2)* [1996] 1 BCLC 155, 249).

corporate interests and shareholders' interests are necessarily, or ought to be always, one and the same is implicitly rejected. Further, the company's interests as a distinct commercial entity are regarded as worthy of protection even if doing so is at the expense of shareholders' interests.

Moreover, while the court recognises corporate interest as distinct and separate from shareholders' interests, it also acknowledges that that is not the only way to understand corporate interest. The court states that in other contexts, the interests of a company may (but not must or should) overlap with those of shareholders as a whole.[53] In doing so, the court understood that corporate interest falls within a spectrum that varies with contexts. This is a nuanced appreciation that solvent companies can have different purposes and interests and the law can accommodate and facilitate them. This is an implicit repudiation of the view that the interests of the company are necessarily, solely or primarily identified, or ought to be identified, with those of shareholders.

This is also the statutory position under Singapore law. Neither the shareholder primacy nor the enlightened shareholder value approach is reflected in s 159(a) of the Singapore Companies Act which permits directors to have regard for 'the interests of the company's employees generally, as well as the interests of its members'[54] when they exercise their powers. It is important to note three differences between this provision and s 172(1) of the UK Companies Act. First, s 159 allows directors to take into account the employees' interests without requiring them to do so for the shareholders' benefit, in contrast to s 172(1). In other words, directors can have regard to the employees' interests not as means to promote shareholders' interests but arguably as an end in itself. Second, it is telling that in terms of the order of interests to which directors can have regard, employees come first followed by

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[53] *Raffles Town Club Pte Ltd v Lim Eng Hock Peter* [2010] SGHC 163 [163].

[54] This language is identical to s 309(1) of the UK Companies Act 1985.

shareholders. By contrast, the primacy of shareholders' interests is evinced in the language of s 172(1) which starts off by mandating directors to promote the company's success for the shareholders' benefit which is followed by the requirement that 'in doing so' directors need to have regard to the interests of stakeholders. Third, s 159 is permissive and agnostic: it permits but does not require directors to have regard for the interests of employees and shareholders. Further, s 159 does not preclude directors from having regard to other types of interests such as those of the company as a distinct commercial entity, suppliers, creditors, etc. Section 159 is also agnostic in relation to corporate interest (whether shareholder primacy, stakeholder or something else), unlike s 172(1), which explicitly endorses an enlightened shareholder value approach.[55]

Finally, the Singapore Code of Corporate Governance states that directors are fiduciaries who act objectively in the best interests of the company but it does not specify the meaning of that phrase.[56] Listed companies are required under the listing rules to disclose in their annual reports their corporate governance practices and any deviations from the Code. Any interpretation and implementation of what it means to act in the company's interests in the Code must be exercised in light of the law, as examined above. On this view, it is not only unnecessary for directors to equate the interests of the company with those of shareholders, but they could, in certain circumstances, prefer the interests of the company as a separate commercial entity (or possibly even non-shareholders) over those of the shareholders. On another view, however, although the Code does not explain the meaning of the company's interests, there is language in the Code that gives prominence to shareholders' interests. It is stated that an aim of corporate governance is to 'enhance long-term shareholder value, whilst

[55] But where the company is insolvent or near-insolvent, directors are required to take into account the interests of creditors which are paramount and overriding. The Singapore position in this regard is identical to that of the UK.

[56] Code of Corporate Governance, 6 August 2018, Principle 1.1.

taking into account the interests of other stakeholders.'[57] However, there is also language that suggests that shareholders' interests are distinct from corporate interest. For example, it is stated that 'performance-related remuneration is [to be] aligned with the interests of shareholders and other stakeholders *and promotes the long-term success of the company.*'[58] Another example is that the Code states that the board is responsible for the long-term success of the company.[59] Moreover, it is stated that the board has to put in place internal control systems to 'safeguard the interests of the company and its shareholders.'[60] In any event, the Code can be read as agnostic and permissive as to the purposes and interests that the company should pursue. This is because the Code does not specify what long-term success means, and although the Code states that the board has to put in place mechanisms so that the company can meet its objectives, no mention is made of what those objectives are. This interpretation is in line with the case law and s 159.

ii. Malaysia

Section 213(1) of the Malaysia Companies Act 2016 states: 'A director of a company shall at all times exercise his powers in accordance with this Act, for a proper purpose and in good faith in the best interests of the company.'[61] Unlike s 172(1) of the UK Companies Act, the Malaysian provision does not specify for whose benefit directors have to act; nor does it

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[57] Ibid Introduction, para 1.

[58] Ibid Provision 7.1 (emphasis added).

[59] Ibid Principle 1.

[60] Ibid Principle 9.

[61] Malaysia Companies Act 2016 (MY CA), s 213(1).

state whether directors can have regard to the interests of stakeholders and if so, which ones. Unlike s 166(2) of the Indian Companies Act which requires directors to act in the best interests of the company, employees, shareholders, the community and environment, the Malaysia provision only requires directors to act in the company's best interests. The language of s 213, thus, does not mandate the pursuit of any particular corporate interest, unlike UK's s 172(1) or India's s 166(2).

As to what is meant by the company's interests (in s 132 of the Malaysia Companies Act 1965 which is the precursor of s 213, the latter of which is identical to the former), the Malaysian Court of Appeal held that '… the duty to act in the best interest of the company means different things, depending on the factual circumstances. Consequently, depending on the type of dispute or issue, the directors must place a higher priority on the interest of the persons who are truly affected.'[62] On the facts of the case, the court held that because the shareholders, not the company, would be most affected had the directors not decided the way they did, the directors did not breach their duty by acting for the shareholders' benefit when they made the decision.[63]

The court's reasoning is significant. First, the court's context-sensitive approach towards determining what constitutes the interests of the company is inconsistent with the English common law position under which corporate interest is necessarily equated with shareholders' interests. Further, not only is it apparent from the court's reasoning that s 213 does not require directors to pursue any particular corporate interest, but s 213 also permits

[62] *Pioneer Haven Sdn Bhd v Ho Hup Construction Company Berhad* [2012] 3 AMR 297, 331.

[63] The parent company, which was listed, was in financial distress and its board executed a joint development agreement between the parent's subsidiary and a third party, under which the latter would finance and develop the project and the subsidiary would be entitled to a certain percentage of the development value. The rationale was that the subsidiary would then issue dividends to the parent company. Had the parent's board not executed this agreement, its financial condition would worsen and it was likely to be delisted.

directors to pursue and prioritise different interests, depending on the circumstances and contexts. Second, the court implicitly affirmed the view that the company has interests that are separate and distinct from those of its shareholders. This is evident when the court said that '[i]n view of Ho Hup's imminent delisting, it stands to reason that the directors were motivated to rescue Ho Hup from being delisted. Thus, in this scenario, the shareholders are most affected, *not so much the company*.'[64] The implication seems to be that should the interests of the company be the most affected, or significantly more so than those of the shareholders, then directors will not be in breach of their duty should they prefer corporate interest over shareholders' interests. This would be consistent with the Singapore case law analysed above. Further, it has been acknowledged that the 'the common law also recognises that the company can also have interest that is separate from the collective interest of its shareholders: *Intraco Ltd v Multi–Pak Singapore Pte Ltd* [1995] 1 SLR 313.'[65]

However, under the 2017 Malaysian Code on Corporate Governance, 'the ultimate objective' of corporate governance is defined as 'realising long-term shareholder value while taking into account the interest of other stakeholders.'[66] This is subsequently reiterated in the Code as follows: 'Corporate governance is not only concerned with shareholder interests but requires balancing the needs of other stakeholders such as employees, customers ...'[67] This is essentially the UK enlightened shareholder value approach. Large listed companies are required to apply the principles in the Code, report whether and the extent to which they have done so, but if they are not able to implement the principles, they are required to come up with

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[64] *Pioneer Haven Sdn Bhd v Ho Hup Construction Company Berhad* [2012] 3 AMR 297, 331.

[65] The Malaysian Corporate Law Reform Committee for the Companies Commission, *A Consultative Document on Clarifying and Reformulating the Directors' Role and Duties* (August 2006), fn 67, p.58.

[66] Malaysia Code on Corporate Governance (April 2017) para 1.1.

[67] Ibid para 1.2.

alternatives as to how they will meet the intended outcomes sought to be achieved by the principles.

However, tellingly, none of the principles in the Code states that directors have to maximise shareholder value. Thus, companies can apply these principles without necessarily adopting the enlightened shareholder value approach. This is because these principles are essentially processes or procedures that do not mandate the pursuit of any particular corporate purpose and interest. For example, Principle A states that at least half of the board should consist of independent directors.[68] The Code states that the 'intended outcome'[69] of this principle is to enable directors to act in the best interests of the company. Yet, the company's best interests are nowhere defined in the Code. While it is possible for companies that are bound by the Code to make reference to paragraph 1.1 which espouses the enlightened shareholder value approach, it is also possible for companies to identify the best interests of the company with those of a commercial entity that are distinct and separate from shareholders' interests. Nothing in the principles themselves obliges companies to adopt a shareholder value maximisation/enlightened shareholder value approach.

iii. India

In India, s 166(2) of the Companies Act 2013 stipulates: 'A director of a company shall act in good faith in order to promote the objects of the company for the benefit of its members as a whole, and in the best interests of the company, its employees, the shareholders, the

[68] Ibid para 4.1.

[69] Ibid para 4.0.

community and for the protection of environment.'[70] There are two interpretations of this provision. The first is based on the report of the Parliamentary Standing Committee on Finance which was in charge of drafting the provision, which indicates that directors are required to act in good faith for the purpose of advancing the company's objects in order to benefit the company and all the stakeholders.[71] On the second interpretation, which is based on a natural and ordinary construction of the provision, directors have to act in good faith both (a) to promote the company's objects *and* (b) in the best interests of the company and all the stakeholders (including shareholders).

There are three common features in both interpretations. First, similar to the case law in Singapore, the interests of the company are distinguished from those of the shareholders and non-shareholders. This is reflected in the language '… in the best interests of the company, its employees, the shareholders …'. Further, s 166(2) requires corporate interest to be protected. Second, unlike s 172(1) of the UK Companies Act, the requirement to act in the interests of non-shareholders (i.e. the employees, community and environment) is not a means to benefit the shareholders. On the contrary, the wording suggests that directors have to act in the interests of all constituencies (employees, shareholders and the community). The third and final commonality is that both interpretations reject the shareholder primacy and enlightened shareholder value approaches. Instead, based on the Standing Committee Report and the wording of the provision, a pluralist stakeholder approach is espoused.

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[70] S 166(2) India Companies Act 2013.

[71] Twenty-first Report, Standing Committee on Finance (2009-2010) (Fifteenth Lok Sabha), The Companies Bill, 2009 (Ministry of Corporate Affairs), Lok Sabha Secretariat, New Delhi (31 August 2010), para 11.80 < http://www.prsindia.org/uploads/media/Companies%20Bill%202009.pdf> accessed 1 December 2018; Mihir Naniwadekar and Umakanth Varottil, 'The Stakeholder Approach Towards Directors' Duties Under Indian Company Law: A Comparative Analysis' (11 August 2016) 10 <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2822109> accessed 1 December 2018.

The main difference, however, between the first and second interpretation is that under the second interpretation, there is a separate duty to act in the interests of stakeholders. By contrast, on the first interpretation, the Standing Committee stated that there is only one duty which is to promote the objects of the company and directors have to do so in the best interests of the company and all the constituencies.

It is suggested that the second interpretation is more persuasive than the first. This is because if the first interpretation were correct, this would render the phrase 'and in the best interests of the company… environment' redundant. Further, the second interpretation is consistent with s 149(8) of the Companies Act 2013 which requires independent directors to comply with the Code for Independent Directors under which they are obliged to 'safeguard the interests of all stakeholders…' [72] and to 'balance the conflicting interest of the stakeholders.'[73] Nevertheless, as there appears to be no case law yet on s 166(2) or 149(8), it remains uncertain whether the first or second interpretation is the correct one.

If the court were to hold that the second interpretation is the correct one, although it is highly doubtful that non-shareholders (such as the employees and community) can enforce the duties[74], the effect of s 166(2) is not entirely diminished. This is because it is suggested that on either the first or second interpretation, directors will not be in breach of their duty should they give greater weight to the interests of the company or non-shareholders (such as employees) than those of shareholders; nor will they be in breach should they prefer corporate interest or non-shareholders' interests where these interests conflict with those of shareholders. This is

[72] Schedule IV, para II(5).

[73] Schedule IV, para II(6).

[74] First, nothing in s 166(2) or the rest of the statutory provisions detracts from the fundamental rule that director's duties are owed to the company and hence only the company (acting through its board or the shareholders under a derivative action) can enforce the duties. Second, it is unlikely that Parliament intended to give the right to sue to a stakeholder that is as nebulously defined as "community" or "the environment". Naniwadekar (n 71) 13-18.

because under s 166(2), directors only have to subjectively believe in good faith that they have acted in the best interests of the company and stakeholders.[75]

That said, the important thing to bear in mind is that the aim of the analysis here is not to evaluate whether the pluralist stakeholder approach or enlightened shareholder value approach is better, nor is it to evaluate the effectiveness of s 166(2). Rather, the aim is twofold: first, to show that as a matter of Indian law, the interests of the company are not equated solely or predominantly with those of shareholders; and second, to show that Indian law requires the protection and promotion of corporate interest that is distinguished from the shareholders' interests. Indeed, whether we adopt the interpretation favoured by the Standing Committee or the one based on a natural construction, it is evident that under s 166(2), the company has interests that are distinct and separate from its shareholders and stakeholders. Further, on either interpretation, not only are the interests of shareholders not prioritised ahead of those of other stakeholders, but the view that the company's interests are equated with the shareholders' interests is also rejected.

iv. Hong Kong

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[75] The subjective nature of this duty may be vulnerable to the criticism that because directors are not held accountable to any specific persons, they can conceal their use of this provision for their own personal benefit at the expense of the company and stakeholders under the veneer of balancing and giving effect to all the stakeholders' interests. But this criticism can be rebutted because courts have reviewed directors' assertions that have acted in good faith according to an objective, reasonable benchmark. In *Simtel Communications Ltd v Rebak* [2006] 2 BCLC 571 [104], although the director asserted that he had considered the company's best interests, the court held that the director was liable for breaching the duty because "[a]n intelligent and honest man in the position of [the director] could not, in the whole of the circumstances, have reasonably believed that these transactions were for the benefit of Simtel."[75] In short, the standard of director's conduct is subjective but the standard of judicial review is objective: Ernest Lim, "Judicial Intervention in Directors' Decision-Making Process: Section 172 of the Companies Act 2006" [2018] *Journal of Business Law* 169.

As compared to the other three Asian jurisdictions, Hong Kong's legal position with regards to the company's interests mirrors the English common law position, namely, the interests of all the shareholders, current and future.[76] Tellingly, the authors of the leading textbook on Hong Kong company law state that '[g]enerally, the interests of shareholders will be their financial interests flowing from maximisation of the company's profits…'[77] Hong Kong law can be criticised for failing to understand that corporate interest depends on context such as the nature and objective of the business in light of economic and industry conditions, all of which implies that it is not always appropriate to require directors to act for the shareholders' benefit given that other interests of other constituencies may warrant greater attention.

It might be argued that Hong Kong law not only does not bar companies from considering the interests of non-shareholders, but non-shareholders' interests are also likely to be considered, if not, protected, when directors act in the interests of future shareholders. This is theoretically true. But two points should be noted. First, where there is a conflict of interests between the shareholders and non-shareholders, the former would be preferred. Absent any conflict, the interests of non-shareholders in a solvent company are necessarily subordinated to those of shareholders. Second, in reality, given that only the current and not future shareholders wield voting powers (particularly the power to remove and appoint directors), it is likely that directors will act in the interests of the current shareholders for the latter will take precedence over those of the future shareholders. This is likely to disincentivise directors to protect the long-term interests of both present and future shareholders, thereby potentially resulting in a strategy of short-termism. It is suggested that Hong Kong courts should consider adopting the

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[76] Hong Kong Companies Registry, *A Guide on Directors' Duties* (2009), Principle 1; Stefan HC Lo and Charles Z Qu, *Law of Companies in Hong Kong* (2nd ed, Sweet & Maxwell 2015) [8.030].

[77] Lo and Qu, ibid.

Singapore and Malaysian position which recognises that corporate interest is context-dependent: while it can refer to the interests of shareholders as a whole, it can, in other contexts, refer to the interests of the company itself that are separate and distinct from the shareholders and stakeholders.

Finally, Hong Kong did consider whether to adopt the UK s 172(1) but rejected doing so because, among the reasons given, s 172(1) was unclear and difficult to comply with, directors would be heavily burdened, potential independent directors would be discouraged to take up the post, and enlightened shareholder value concept has not gained traction in Hong Kong.[78]

v. Implications

Although the law gives significant powers to shareholders in the UK and the four common law jurisdictions in Asia, there is a marked divergence in the way the law prioritises the interests of shareholders and other stakeholders. Under English law, shareholders are not only given considerable powers but their interests are given paramount status under s 172(1).[79] By contrast, in India, Singapore and Malaysia, it does not follow from the significant powers of shareholders that their interests would be accorded the same status or weight. In India, not only is shareholder primacy explicitly rejected, but the interests of shareholders are merely one

[78] Public Consultation on Company Names, Directors' Duties, Corporate Directorship and Registration of Charges Compendium of Responses <http://www.fstb.gov.hk/fsb/co_rewrite/eng/pub-press/doc/cdrc_compendium_e.pdf.> accessed 1 December 2018.

[79] Note that although s 172(1) reflects an enlightened shareholder value approach, companies are not required to pursue this approach. Section 172(2) states 'where or to the extent that the purposes of the company consist of or include purposes other than the benefit of its members, subsection (1) has effect as if the reference to promoting the success of the company for the benefit of its members were to achieving those purposes.' This means that if companies have a purpose that is other than to benefit the members, then directors are obliged to pursue that purpose. See explanatory note to s 172(2).

of the categories of protected interests under s 166(2); shareholders do not have a superordinate status. In Singapore and Malaysia, whose interests – whether those of the company, shareholders, or non-shareholders - should be preferred where there are conflicts, are context dependent. In short, whose interest will be protected is usually a consequence of who wields the power, as is the case in the UK and Hong Kong. But that is not the case in India, Malaysia and Singapore.

First implication: it is not circular for controlling shareholders to act in the interests of the company

The legal analysis has two vital implications for what it means for controlling shareholders to act in good faith in the best interests of the company. First, it rebuts the criticism of circularity by demonstrating that not only is corporate interest distinguished from shareholders' interests, but corporate interest can also, and in the case of India is required to, be protected and promoted. Thus, controlling shareholders can prioritise and prefer corporate interest where there is a conflict between the latter and the interests of shareholders. In many circumstances, protecting and promoting the interests of the company will also protect shareholders' interests. After all, shareholder prosperity is an outcome of corporate success. Shareholder gain derives from or is reflective of corporate gain. But this is not case when the interests of the controller conflict with those of the company.

Second implication: the laws of three Asian jurisdictions are consistent with my position that corporate interest refers to the long-term value and viability of the company

The second implication of the comparative legal analysis is that Singapore, Malaysian and Indian law is consistent with my position: the notion of the interests of the company refers to the long-term value and viability of the company, which permits taking into account the interests of shareholders and other stakeholders but is not equated with any particular constituency. And where there is a conflict between the interests of the company on the one hand, and the interests of shareholders on the other hand, the long-term value and viability of the company requires, and Singapore and Malaysian law allows, the corporate interest to be given effect to. While Indian law does not tell us whose interests should be preferred when the interests of the company conflict with those of shareholders, employees or the community, it is suggested that there should not be a breach of fiduciary duty simply because corporate interest is preferred over the shareholders' interests if the circumstances of the particular case warrant doing so.

However, it may be said that the English common law position, on which Hong Kong law is based, already permits and possibly requires non-shareholders' interests to be considered and even protected because the interests of the company have been equated with those of the future shareholders (in addition to current shareholders), which implies long-term corporate interest, the implementation of which requires the consideration and even protection of non-shareholders' interests. Although this sounds plausible in theory, it is unlikely to be the case in practice.[80] After all, only the current shareholders, not the future shareholders, have voting powers, and directors are unlikely to oppose the wishes of those who wield the power to dismiss them. Further, the nature and scope of the interests of "future" shareholders remain obscure.

[80] For example, the codified version of the English common law position, s 172, has been understood by directors to maximise share price: Ferran (n 11). Further, the 2012 Kay Review noted that "[m]any of the bad [board] decisions described were supported or even encouraged by a majority of the company's shareholders": (n 10), [1.28].

Thus, under Hong Kong law and English common law, directors are likely in practice to act only or mostly in the interests of the current shareholders, which often translates into maximising share price, which means that the interests of non-shareholders are unlikely to be promoted unless doing so benefits the current shareholders.

In any event, a key difference between the English and Hong Kong legal position, and the laws of Singapore, Malaysia and India is this: under English and Hong Kong law, non-shareholders' interests are taken into account only in order to further shareholders' interests, and non-shareholders' interests are necessarily subordinated to shareholders' interests. Where there is a conflict between the interests of shareholders and those of non-shareholders (in the context of a solvent company), it is clear that the former trumps the latter under Hong Kong and English law. By contrast, the laws of the three countries (Singapore, India and Malaysia) do not require (unlike the UK s 172(1)) the interests of non-shareholders to be taken into account only as a means of advancing shareholders' interests. Further, Indian law explicitly obliges the best interests of the non-shareholders to be promoted as an end in itself, in addition to those of the shareholders. Under the laws of India, Singapore and Malaysia, it is submitted that no interests – whether they are the shareholders' or non-shareholders' – have *a priori* primacy. Non-shareholders' interests are not necessarily subordinated to shareholders' interests. The issue of which constituency's interest should be given priority when conflict arises would depend on the context.

vi. Objections

It may be argued that although Singapore, Malaysian and Indian law supports the argument that corporate interest is independent of shareholders' interests, and that the interests of the company extend beyond those of shareholders to include other stakeholders like employees, it would not make any material difference in reality. This is because only shareholders have the power to enforce the duties owed to the company in a derivative action, and they are the only constituency to have the power to alter the constitution and remove directors who defy their wishes. Where there is a conflict between the interests of the shareholders (who have the voting powers) and non-shareholders (who lack voting powers), or a conflict between corporate interest and shareholders' interests, directors who are elected by shareholders and who can be removed and/or sued by shareholders, will in reality prioritise and act in the latter's interests, even if doing so is at the expense of the company and other stakeholders. After all, those who wield corporate power determine corporate interest.[81] To put it starkly, 'if the only power within the corporate polity is wielded by equity capital, then the ends of governance will maximise equity's preferences.'[82] What this means is that in reality, directors are likely to heed the controlling shareholder's wishes, even if the controller did not exert any pressure on the board. Thus, cases of controlling shareholders being held liable for breaching the best interest duty because they dismiss (or threaten to dismiss) directors for opposing their wishes are likely to be rare.

However, it is difficult for shareholders to succeed in a derivative action against directors for breach of duties (as I will explain in Chapter 6). And the threat of being removed will no longer be a credible one if controlling shareholders are subject to the duty to act in good faith in the best interests of the company when they exercise their appointment and removal powers.

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[81] Leo Strine, Jr, "Corporate Power is Corporate Purpose I: Evidence from my Hometown" (2017) 2 *Oxford Review of Economic Policy* 176, 180 ('power is purpose within the corporate polity').

[82] Leo Strine, Jr, "Corporate Power is Corporate Purpose II: An Encouragement for Future Consideration from Professors Johnson and Million" (2017) 74 *Washington & Lee Law Review* 1165, 1171.

Another objection is that the controlling shareholder could pursue his own agenda at the expense of the company and minority shareholders. This is because under Singapore, Malaysian and Indian law, significant discretion is given to the decision-maker to determine whose interests should prevail where there are conflicts; or even if there are no conflicts, whose interests should be given greater weight. This is the downside of not mandating the pursuit of the interest of a particular constituency as the ultimate objective, unlike the UK s 172.

The rebuttal is that this objection wrongly assumes that a single, overarching metric or goal, such as maximisation of share price, is necessary for the controlling shareholder to discharge his duty to act in the company’s interests. Promoting the long-term value and viability of the company would consist of ensuring that: employees’ interests are attended to (as seen in the hiring, retention and attrition rate as well as employee surveys and feedback), customers are satisfied with the products and services (as shown in the revenue, profitability and customer surveys and feedback), shareholders’ interests are met (as seen in the share price and issuance of appropriate dividends) and contributions are made to the community (as seen in philanthropic activities).

3. Empirical

It is necessary but insufficient that we examine the theories and laws. We should also look at how listed companies in the four countries in Asia have articulated their corporate purposes. I will draw on the data to make several points, but the most important point I wish to make is this: the fact that approximately 39% of the top 30 listed companies in all the four Asian countries have corporate purposes that are not based on shareholder primacy or stakeholder value but are instead based on the protection and promotion of the corporate entity lends empirical support to my central argument in this chapter, i.e. that the notion of the 'interests of the company' — in relation to the duty of the controlling shareholders to act in good faith in the best interests of the company — need not be equated with or reducible to the interests of shareholders or other stakeholders; rather it can be based on the long-term value and viability of the company.

i. Reasons for empirical analysis

a. First analysis of common law Asia

This is the first empirical analysis of corporate purposes of the listed companies in the common law countries in Asia. There has been similar research conducted on the corporate purposes of companies in the UK[83], Australia[84] and Japan.[85] Yet, there appears to be nothing on the common law countries in Asia so far. I categorised the corporate purposes into three categories: shareholder primacy (which includes enlightened shareholder value), stakeholder, and others. I give examples of these three categories below.

b. Whether the law facilitates and is consistent with the company's stated purpose

[83] Andrew Keay and Rodoula Adamopoulou, 'Shareholder Value and UK Companies: A Positivist Inquiry' (2012) 13 *European Business Organization Law Review* 1.

[84] Meredith A Jones and others, *Company Directors' Views Regarding Stakeholders* (Research Report, Faculty of Law, University of Melbourne 2007) <http://cclsr.law.unimelb.edu.au/go/centre-activities/research/research-reports-and-research-papers/ index/cfm> accessed 1 December 2018.

[85] Masaru Yoshimori, 'Whose Company Is It? The Concept of Corporations in Japan and the West' (1995) 28 *Long Range Planning* 33.

Second, it is important to understand whether the law facilitates and is consistent with companies' own articulated purposes. For example, if the law mandates (as opposed to permits) the pursuit of a specific corporate interest (such as shareholder primacy in Hong Kong), but if the majority of the most significant listed companies in the respective jurisdictions view their interests, in light of their stated purposes, differently from that which the law requires of them, this disconnect would impact on the proper functioning of the law and companies.

Based on my research, only 27% of the top 30 listed companies by market capitalisation in Hong Kong defined their objectives in terms of shareholder primacy. The other 33% can be classified as stakeholder value and the remaining 40% is neither shareholder primacy nor stakeholder value. Thus, one concern is whether Hong Kong law does not adequately account for reality and whether a legal approach that explicitly recognises, accommodates and protects a plurality of purposes may be more appropriate for its listed companies. By contrast, in India, only 6% of companies espoused shareholder primacy approach, whereas 47% defined their corporate purpose in terms of stakeholder value. Thus, s 166(2) of the Indian Companies Act seems to be aligned with how the most significant listed companies have already defined their purposes.

Singapore and Malaysian law, in addition to Indian law, recognise and protect the interests of the company as a separate commercial entity. This is consistent with empirical reality: it is interesting to note that a significant percentage of the corporate purposes of companies (40% in Hong Kong, 37% in Singapore, 27% in Malaysia, and 47% in India) reflect neither shareholder primacy nor stakeholder value. In other words, about 39% of all the top 30 listed companies in all the four jurisdictions have corporate purposes that are stated not in terms of shareholder primacy or stakeholder value. I classify such purposes as 'others' and I will elaborate on them below. I will provide one example for now as an illustration. Consider Kuala Lumpur Kepong, a palm oil producer, listed in Malaysia. Its purpose, as stated in its mission statement, is to 'strive to emerge as a global force in the plantations and oleochemical arena and to continue building on the Group's century old legacy of excellence *by*: Offering quality products and services at competitive prices; being a good and responsible corporate citizen; earning a fair return on investment; maintaining steady dividend payments…'[86] Thus, the corporate objective is to be a leader in the area of plantations and oleochemical and the means to attain this objective is to be good to customers (by offering quality products), good to society (by being a responsible corporate citizen) and good to shareholders (by issuing steady dividends). It is evident that acting in the interests of shareholders (or other stakeholders) is but a means not an end; it is a strategy to advance the corporate goal, that is not equated with the interests of any constituency.

The above example of corporate purpose – which I classified as 'others' – illustrates three crucial insights. First, benefit to shareholders and other stakeholders is not the purpose/goal of the company but it is an outcome of the pursuit of corporate purpose. Second, acting in the interests of shareholders or other stakeholders is not an end, contrary to what the enlightened shareholder value or stakeholder model teaches us. It is but a means, a strategy to achieve the goal of promoting and protecting the corporate purpose that is not synonymous with that of any shareholder or stakeholder. Rather, the corporate purpose emphasises the importance of the corporate entity itself. Finally, stakeholder value can be as problematic as enlightened shareholder value in that both approaches require companies to advance the interests of one or more constituencies, as an end itself, and disregards the central and

[86] Kuala Lumpur Kepong Berhad, Corporate Mission & Values < http://www.klk.com.my/corporate-information/corporate-mission-values> accessed 1 December 2018.

overarching corporate purpose, ‘to which those constituencies contribute and from which they benefit, but which is distinct from their individual goals and interests.’[87]

c. Corporate purpose is important to the company’s long-term viability and prosperity

The third reason for the empirical analysis is that because purpose is critical to the long-term viability and prosperity of companies, it is necessary that we understand what the companies’ purposes are. Purpose determines the goals, strategies and values of companies. And crucially, delivering purpose improves the performance of companies. It has been said that ‘[a]n increasing body of evidence, spanning thousands of companies, across dozens of industries and countries, demonstrates a causal relationship between purpose and sustained competitive advantage rather than mere correlation.’[88]

d. Corporate purpose is important to law and policy reform project

The fourth and final reason is that understanding the companies’ avowed purposes is a prerequisite for any meaningful law and policy reform project – what corporate purposes ought to be and how the law and institutions can promote them. Once we ascertain how companies have defined their objectives and goals, it would be helpful to know their reasons for doing so.

[87] Johnson (n 4).

[88] Big Innovation Center, *Purposeful Company: Policy Report* (Feb 2017) 10 <http://www.biginnovationcentre.com/media/uploads/pdf/TPC_Policy%20Report.pdf> accessed 1 December 2018. See the extensive literature cited and summarised in Big Innovation Center, *Purposeful Company: Interim Report* (May 2016) 26-33.

And once we understand the 'what' (the avowed purposes) and 'why' (the reasons for having such purposes), we can proceed to analyse whether, to what extent, and how corporate purposes can and ought to be reformed.

ii. Methodology

I have selected the top 30 listed companies by market capitalisation in each of Singapore, Malaysia, Hong Kong and India. The 30 companies in each of these four countries constitute 61%, 58%, 54% and 46%, respectively, of the total market capitalisation of all the listed companies in each of the respective jurisdictions.[89] As a result, these 30 companies in each of the four countries constitute a majority or close to a majority of the total market capitalisation of all the listed companies. Market capitalisation is evidence of the size and impact of the company.[90] Analysing the avowed corporate purposes of these companies should therefore provide a reasonably reliable source of information on some of the largest and most significant companies in these four countries. Table 2 lists out the names of the top 30 companies in each of the four countries.

To discern the purposes of these companies, I have examined the publicly disclosed documents including the annual reports, the mission statements, websites, the corporate social responsibility reports, as well as environmental, social and governance reports, placing particular weight on annual reports which are usually considered the most important and

[89] Based on hand collected data, the percentages are calculated by adding the market capitalisation of the top 30 companies divided by the total market capitalisation of all the listed companies, as of 10 January 2018.

[90] George A Fontanills and Tom Gentile, *The Stock Market Course* (John Wiley & Sons Inc. 2001) 206.

comprehensive source of communication by and on the companies. Table 3 shows all the documents reviewed for the top 30 companies in each of the four jurisdictions.

There are some limitations to the empirical analysis, however. The corporate purposes stated in the annual reports and other publicly disclosed documents are unlikely to be legally enforceable; the analysis only investigates what the companies assert as their purposes and not whether these assertions have been implemented; and some of these statements might even contain puffery and public relations rhetoric.[91]

Nevertheless, the significance of the corporate purposes stated in these documents should not be underestimated. This is because annual reports (i) have been regarded as the most important medium through which the company's objectives, value and strategies are communicated to its stakeholders and the public[92]; and (ii) provide a measure of accountability as the stakeholders and analysts can evaluate the company based on its statements in the annual reports and to put pressure the company should there be any deviation.[93] Mission statements (i) are official declarations made by the company only after very careful consideration[94]; (ii) provide a crucial basis on which to develop the key strategies of the company[95]; and (iii) they identify the key stakeholders in the company who can have a moral claim on the company.[96]

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[91] The process and limitations of the methodology here are drawn from Keay (n 83).

[92] Keay (n 83) 15; Stuartz Goldstein, 'Redefining the Role of the Annual Report' <http://www. stuartzgoldstein.com/articles/role_annual_report.html> accessed 1 December 2018; Feng Li, 'Annual Report Readability, Current Earnings, and Earnings Persistence' (2008) 45 *Journal of Accounting and Economics* 221; Reuven Lehavy and others, 'The Effect of Annual Report Readability on Analyst Following and the Properties of Their Earnings Forecasts' (2011) 86 *Accounting Review* 1087; Jianling Wang and Lin Song, 'Timeliness of Annual Reports of Chinese Listed Companies' (2006) 4 *Journal of Chinese Economic and Business Studies* 241.

[93] Keay (n 83) 15.

[94] Claudio Loderer and others, 'Shareholder Value: Principles, Declarations, and Actions' (2010) 39 *Financial Management* 5.

[95] Mohammed Omran and others, 'Shareholders versus Stakeholders: Corporate Mission Statements and Investor Returns' (2002) 11 *Business Ethics: A European Review* 319.

[96] John A Pearce II, 'The Company Mission as a Strategic Tool' (1982) 23 *Sloan Management Review* 15, 23.

Moreover, with respect to corporate social responsibility reports, as well as environmental, social and governance reports, one cannot rule out the possibility that liability can be imposed on companies for making false and misleading statements in those reports. For example, Nike stated in its corporate social responsibility reports that its suppliers complied with its code of conduct which did not permit sweated labour but an activist discovered that sweated labour was used in the factories that supplied Nike's products and successfully sued Nike for making false statements.[97] This suggests that the statements made by companies in such reports have to be verifiable; otherwise there is a risk of legal liability. This in turn calls into question the criticisms that the claims made by companies in such reports are puffery and hence should not be taken seriously.

One other issue is that the empirical analysis is not entirely devoid of difficulties.[98] It is not always easy to distinguish the means (i.e. the strategies) and ends (i.e. the ultimate purpose). Differentiating the ultimate purpose from the series of purposes that comprise or lead to the ultimate purpose can be tricky at times. Another difficulty is that the mission statement may contain different purposes (that reflect stakeholder value, enlightened shareholder value and real entity approach) and the question is which is the ultimate or predominant one. Judgment is required when the assertions in the mission statement, the annual report or other reports (such as the corporate governance report or CSR report) do not appear to be identical: the difficulty lies in discerning whether the deviation is apparent or real or whether it is merely a question of emphasis.

An illustration of some these difficulties, albeit not common, can be found in Singapore Telecommunications Limited, which has the second highest market capitalisation, listed in

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[97] *Kasky v Nike, Inc.*, 45 P 3d 243 (Cal. 2002).

[98] Keay (n 83) 13.

Singapore. Under the 'Mission' section in the 2015 Annual Report, it is stated: 'We believe that the world is a better place when technology is used to help people and businesses communicate effortlessly. We make communication easier, faster, and more reliable for customers, while delivering value to our stakeholders.'[99] The corporate purpose as defined would thus suggest a stakeholder value approach. However, in the same annual report, under the section 'Our Strategy', it is stated: '*Our goal*: create sustainable long-term growth *to* deliver superior returns to shareholders. Our Strategy: strengthen the core business and build new growth engines.'[100]

If one interprets the statement made under 'Our goal' as the purpose of the company, then the wording – '*to* deliver superior returns to shareholders' - appears to be the ultimate purpose, which in turn suggests a shareholder primacy approach. The intermediate purpose is to 'create sustainable long-term growth'. The corporate purpose as reflected under 'Our Goal' is inconsistent with the corporate purpose stated in the 'Mission' section in the 2015 annual report statement. But these statements cannot be read in isolation. They have to be read in light of other annual reports and the sustainability reports. There are statements from the Chairman and Group CEO in the 2016 and 2015 Annual Reports about creating value, but they are mostly with reference to shareholders. Further, those reports and the 2016 and 2015 Group Sustainability Reports contain many statements about the aim to 'create long-term growth for our business'. Crucially, the order and priority in which the objectives are placed is also telling. For example, in the 2016 Group Sustainability Report, it is stated: 'We strive to create long-term growth, deliver great customer experience and embrace responsible business practices, be an employer of choice, manage our environmental footprint, and invest the communities we

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[99] Singapore Telecommunications Limited, 2015 Annual Report, 1 <http://info.singtel.com/annualreport/2015/assets/files/Singtel_AR2015.pdf> accessed 1 December 2018.

[100] Ibid 5.

operate.'[101] The order of the objectives suggests that creating long-term growth is the top priority. And, crucially, the 2015 Annual Report specifies that the purpose of creating long-term growth is 'to deliver superior returns to shareholders'. Accordingly, I categorised the ultimate corporate objective of Singapore Technologies as enlightened shareholder value.

In light of these difficulties, the approach that I have taken is to analyse all the relevant publicly disclosed documents with a view to discerning which purpose is given the top priority, whether it is the ultimate purpose, as well as whether and how much emphasis is placed on that purpose. I also distinguished the purposes/goals and the means/strategies. No statement is analysed in isolation and all the relevant statements are corroborated. For example, the largest company in India by market capitalisation, Tata Consultancy Services, states: '[o]ur mission to is help customers achieve their business objectives by providing innovative, best-in-class consulting, IT solutions and services and to make it a joy for all stakeholders to work with us.'[102] The ultimate objective is to help customers achieve their business goals. The strategy to achieve this objective is to provide the best consultancy IT solutions. Overall, the objective can be classified as stakeholder value.

iii. Findings

The tables below show the categorisation of the purposes of the top 30 listed companies in each of the four countries (Singapore, India, Malaysia and Hong Kong) and the percentage

[101] Singapore Telecommunications Ltd., 2016 Group Sustainability Report, 10 <http://info.singtel.com/sustainabilityreport2016/files/Singtel_Sustainability_2016.pdf> accessed 1 December 2018.

[102] Tata Consultancy Services Limited, 2015-2016 Corporate Sustainability Report, 10 <https://www.unglobalcompact.org/system/attachments/cop_2016/334081/original/GRI_Report_FY16_Final.pdf?1478087461> accessed 1 December 2018.

of the companies within each jurisdiction that subscribes to those purposes. The information in the first column is drawn from the findings of Keay and Adamopoulou where they examined the corporate purposes of 50 of the FTSE 100 companies.[103]

Corporate Purpose	UK (%)	Singapore (%)	India (%)	Malaysia (%)	Hong Kong (%)
Shareholder Primacy/Enlightened Shareholder	36	20	6	30	27
Stakeholder	20	43	47	43	33
Others	44	37	47	27	40

Corporate Purpose: Others	Singapore	India	Malaysia	Hong Kong
Leadership	X	X	X	X
Growth	X	X	X	X
State-oriented		X		X

Table 4 shows how the 30 companies in each of the four countries are categorised.

a. Corporate purpose in terms of shareholder primacy

[103] Keay (n 83) 28.

There are several interesting findings that have emerged from the empirical research. First, in none of the jurisdictions is shareholder primacy/enlightened shareholder value the dominant stated corporate purpose. On the contrary, in three of the four common law countries in Asia, it is the minority: 6% in India, 20% in Singapore and 27% in Hong Kong. In Malaysia, it amounts to 30%, which is still lower than the companies that define their corporate purpose in terms of stakeholder value approach (43%).

An example of shareholder primacy corporate purpose can be found in China Mobile, the PRC state-owned enterprise listed in Hong Kong which has the second highest market capitalisation and the world's largest mobile operator. In its 2015 Annual Report, the Chairman stated that '…we will be able to create a robust company … with an aim to deliver strong performance to our shareholders.'[104] In its Corporate Governance Report, it stated that 'the company's established principle is to strive to create value and bring favourable returns for shareholders'[105] and 'our goal has always been to enhance our corporate value, maintain our sustainable long-term development and generate greater returns for our shareholders.'[106] In virtually all of the companies whose corporate purposes are defined in term of shareholder value, they subscribed to the enlightened shareholder model. By way of illustration, CITIC Limited, a multinational conglomerate listed in Hong Kong, stated on its website that it 'aims to generate sustainable shareholder value over the long-term, and we recognise that effective management of stakeholder relationships, including those with investors, is key to realising

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[104] China Mobile Limited, 2015 Annual Report, 15 <http://www.chinamobileltd.com/en/ir/reports/ar2015.pdf> accessed 1 December 2018.

[105] Ibid 42.

[106] China Mobile Limited, Corporate Governance <http://www.chinamobileltd.com/en/about/cg.php> accessed 1 December 2018.

that value.'[107] The Chairman said: 'Core to our success has been our constant pursuit of three fundamental goals: to strive to be the leader in the fields in which we operate, to uphold strong corporate governance and to make our company a place where all employees are eager to work. But most of all, our guiding principle has always been: to create long-term value for all of our shareholders.'[108] It is clear that the 'three fundamental goals' are actually intermediate purposes that are subordinated to the overarching, ultimate purpose which is to generate 'long-term value for all shareholders.'[109]

b. Corporate purpose in terms of stakeholder value

Second, a significant percentage of the listed companies in the common law countries in Asia defined their corporate purpose in terms of stakeholder value. Stakeholder value accounts for the highest percentage among the three types of corporate purpose in Singapore (43%) and Malaysia (43%). An example of corporate purpose that is defined in terms of stakeholder value can be seen in Thai Beverage Public Company Limited that is listed in Singapore. Its mission statement is 'to build strong mutually beneficial relationships with all stakeholders in every aspect…' Another example of stakeholder value corporate objective can

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[107] CITIC Limited, Investor Relations <http://www.citic.com/InvestorRelations/InvestorRelations> accessed 1 December 2018.

[108] CITIC Limited, Chairman's Message <http://www.citic.com/AboutUs/ChairmansMessage accessed 1 December 2018.

[109] Ibid.

be found in Singapore Airlines' mission statement: "Singapore Airlines is a global economy dedicated to providing air transportation services of the highest quality and to maximising returns for the benefit of its shareholders and employees."[110] Among Malaysia's top 30 listed companies, Genting is a good example of stakeholder value corporate purpose. It stated in its mission statement that it will be 'responsive to changing demands of our customers …; generate a fair return to our shareholders; pursue personnel policies which recognise and reward performance and contributions of employees…'[111] Notably, as compared to the other three countries in Asia, India has the highest percentage of companies whose corporate purpose is defined in terms of stakeholder value. For example, Mahindra & Mahindra, an automobile manufacturing company listed in India, defined its 'core purpose' as to 'challenge conventional thinking and innovatively use all our resources to derive positive change in the lives of our stakeholders and communities across the world…'[112]

c. Corporate purpose in terms of the corporate entity (others)

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[110] Singapore Airlines Limited, 2016 Annual Report, Preface <https://www.singaporeair.com/saar5/pdf/Investor-Relations/Annual-Report/annualreport1516.pdf> accessed 1 December 2018.

[111] Genting Berhad, 2016 Annual Report, 1 <http://www.genting.com/wp-content/uploads/2017/07/2016.pdf> accessed 1 December 2018.

[112] Mahindra & Mahindra Ltd., 2014-2015 Annual Report, 36 <http://www.mahindra.com/resources/pdf/homepage/M&M%20Annual%20Report%202014-15.pdf> accessed 1 December 2018.

The third and final finding concerns the corporate purpose that is categorised as ‘others’. These corporate purposes prioritise the interests of the company as a distinct and separate commercial entity. In Singapore, corporate purpose that is defined as ‘others’ accounts for the second highest percentage (37%) after stakeholder value (43%). In India, it is on par with the stakeholder value (47%). In Hong Kong and the UK, it constitutes the highest percentage (40% in the former and 44% in the latter). These corporate purposes emphasise the values of leadership, growth or the state. The purpose of these companies is to promote the interests of the company by making it the leading organisation in its field, by enhancing its growth, and by defining corporate interests in terms of promoting the goals of the state. I will illustrate with examples below. These companies whose corporate purpose that I have classified as ‘others’ mainly seek to promote corporate interest, which is not equated with and is distinct from the interests of shareholders and other stakeholders.

Examples of leadership-based corporate purpose include Ping An Insurance in Hong Kong, and Power Grid Corporation of India. Ping An Insurance stated that it is ‘dedicated to’ and ‘has set the goal of becoming a world-leading personal financial services provider.’[113] Power Grid Corporation of India defines its mission as this: ‘We will become a Global Transmission Company with Dominant Leadership in Emerging Power Markets with World Class Capabilities.’[114] And to achieve this dominant position, Power Grid Corporation listed out eight ‘objectives’ (such as to ensure the development and operation of efficient transmission lines and systems and to restore power quickly in the event of natural disasters).

[113] Ping An Insurance (Group) Co. of China, Ltd – H Shares, 2014 Annual Report, Preface <http://www.irasia.com/listco/hk/pingan/annual/ar139851-e101.pdf> accessed 1 December 2018.

[114] Power Grid Corporation of India Ltd, Vision & Mission <https://www.powergridindia.com/vision-mission> accessed 1 December 2018.

It is clear that these 'objectives' are merely means/strategies to achieve the ultimate or overriding aim to be a global transmission company.

An example of growth centred corporate purpose is HSBC Holdings, listed in Hong Kong, which declares: 'Our purpose is to be where growth is, enabling businesses to thrive and economies to proper, and ultimately helping people to fulfil their hopes and realise their ambitions.'[115] Although the word 'ultimately' may suggest that its corporate purpose is stakeholder value, HSBC clarified that its 'ambition' is 'to be recognised as the world's leading and most respected international bank'[116], and it will 'achieve this by focusing on the needs of [its] customers and the societies [it] serves, thereby delivering long-term sustainable value to all of [its] stakeholders.'[117] Thus, acting in the interests of customers and society at large is but a means or strategy. The word 'thereby' refers to the consequence of focusing on customers' and society's needs rather than the ultimate goal.

MISC, a listed company in Malaysia and one of the leading global tanker operators has repeatedly emphasised the importance of sustainable growth in different places in its annual reports. It describes its mission in this way: 'To consistently be better [in providing energy related maritime solutions and services], we strive: to exceed the expectations of our customers; to promote individual and team excellence of our employees; to care for the environment and operate responsibly; to drive sustainable value of our shareholders.'[118] It is clear that promoting

115 HSBC Holdings Plc, 2016 Annual Report, Preface < http://www.hsbc.com/investor-relations/group-results-and-reporting/annual-report> accessed 1 December 2018.

116 HSBC Holdings Plc, 2015 Annual Report, 12 <http://www.hsbc.com/investor-relations/group-results-and-reporting/group-reporting-archive/quick-read> accessed 1 December 2018.

117 Ibid.

118 MISC, Mission Statement <http://www.misc.com.my/about/> accessed 1 December 2018.

the interests of these constituencies is a means to further its objective of providing better maritime solutions.

Finally, corporate purpose is also defined with reference to the state. Although it is not uncommon for the state as a controlling shareholder of state-owned enterprises/government-linked companies to advance its political and social agenda, seldom do these companies explicitly and forcefully articulate their corporate purpose by directly connecting it with that of the state as is the case in India. For example, ITC, a large conglomerate that has businesses in consumer goods and hotels, states in its Annual Report that: 'ITC is driven by its inspiration to be an exemplary Indian enterprise serving larger national priorities.'[119] 'At ITC, the credo of Country before Corporation defines the Company's nation-orientation, and its aspiration to contribute to a future of rapid progress and prosperity.'[120] Another company, Indian Oil Corporation, declares that 'Indian Oil, which defines itself as The Energy of India, has since inception aligned its corporate strategies with the greater good of the country and its people.'[121] Another company, Housing Development Finance Corporation Ltd, the leading company that provides financing for housing, states that the 'government's mission to provide 'a home for every one' by 2022 mirrors perfectly the ethos and vision of HDFC.'[122] It states that its 'primary objective'[123] is to 'enhance the residential housing stock in the country through the

[119] ITC Ltd., 2015-2016 Annual Report, foreword <http://www.itcportal.com/about-itc/shareholder-value/annual-reports/itc-annual-report-2016/pdf/ITC-Report-and-Accounts-2016.pdf> accessed 1 December 2018.

[120] Ibid.

[121] Indian Oil Corporation Ltd., 2015-2016 Annual Report, 3 <https://www.iocl.com/AboutUs/AnnualReports/AnnualReport201516.pdf> accessed 1 December 2018.

[122] Housing Development Finance Corporation Ltd., 2014-2015 Annual Report, inside front cover <https://www.hdfc.com/sites/default/files/HDFC%20Annual%20Report%202014-15.pdf> accessed 1 December 2018.

[123] Housing Development Finance Corporation Ltd., About us <https://www.hdfc.com/> accessed 1 December 2018.

provision of Housing Finance in a systematic and professional manner, and to promote home ownership.'[124]

Given that companies have defined their purposes with reference to the state's goals, and more importantly, as demonstrated in Chapter 3, because state-owned enterprises/government-linked companies in the common law countries in Asia have pursued political, social and non-financial goals (instead of shareholder wealth maximisation), it is descriptively misleading to equate the interests of the company solely or predominantly with the maximisation of share price. More importantly, the state-oriented purpose of these companies can be consistent with, and is encompassed within, the notion of the interests of the company advanced in this chapter, i.e. the long-term value and viability of the company. As examined in the 'Normative' section, the long-term value of the company is not defined in terms of shareholder value maximisation. Rather, enhancing the company's long-term value and viability will include (but is not limited to) protecting the interests of the employees and consumers. Thus, when the state as a controlling shareholder uses the company to create jobs and reduce prices of goods, these measures will benefit the employees and consumers, which will in turn generate goodwill and brand loyalty among these people. There are also other reasons why companies whose interests are linked to the state could be consistent with the long-term value and viability of the company. This is because these companies tend to be long-term oriented in their strategies and operations, receive government assistance, and will be recapitalised by the government should they be in financial difficulty.[125]

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[124] Ibid.

[125] Nicholas Kaldor, 'Public or Private Enterprise – the Issues to be Considered' in William J Baumol (ed), *Public and Private Enterprises in a Mixed Economy* (Palgrave Macmillan 1980) 1-12; Gerald A. McDermott, *Embedded Politics: Industrial Networks & Institutional Change in Postcommunism* (University of Michigan Press 2003); Aldo Musacchio, 'Sovereign Wealth Funds: Barbarians at the Gate or White Knights of Globalization? (TN)' Harvard Business School Teaching Note 713-075, March 2013. Although the state's interests can be consistent with the long-term value and sustainability of the company, it can also be in tension because of inefficiencies, cronyism and even corruption: see Chapter 3.

To conclude, the empirical analysis supports my central argument. The fact that 39% of the top 30 listed companies in all the four countries in Asia have publicly articulated their corporate purposes not in terms of shareholder primacy or stakeholder value, but in terms of leadership, growth or state goals lends empirical support to my position in two ways. First, it supports my argument that corporate interest need not be equated with shareholder primacy or stakeholder value. Second, and more importantly, the data is consistent with, and elucidates, my position that corporate interest can refer to the interests of the company as a separate and distinct entity, i.e. the long-term value and viability of the company.[126] This is because promoting the long-term value and viability of the company can accommodate the maintenance and enhancement of the leadership position of the company, augmentation of the growth of the company, and the realisation of the economic and social goals of the state.

[126] It might be objected that the data can be read as supporting a position espoused by Oliver Hart and Luigi Zingales, 'Companies Should Maximize Shareholder Welfare Not Market Value' (2017) 2 *Journal of Law, Finance, and Accounting* 247 that corporate purpose (or interest) should be understood to mean whatever the shareholders want it to mean. However, Hart and Zingales draw a critical distinction between maximisation of shareholder welfare and maximisation of market value. And the latter is associated with shareholder primacy. They endorse the former and reject the notion of shareholder primacy in the sense that managers should be solely or primarily concerned with the maximisation of share price. This is consistent with my position. They argue that managers should promote and protect shareholder welfare, which is concerned with giving effect to sustainability and ethical considerations. This is consistent with my notion of corporate interest understood in terms of the long-term value and viability of the company. And my data shows that there is a significant percentage of companies in the four Asian jurisdictions that have such a corporate purpose. This can be read as suggesting that controlling shareholders in a significant percentage of the companies do not subscribe to the maximisation of share price, and managers should give effect to the purpose that is favoured by the controllers, i.e. promoting the interest of the corporate entity, whether defined in terms of enhancing the leadership position of the company, augmenting the growth of the company, or advancing the goals of the government, all of which can be accommodated within the long-term value and viability of the company. This again is consistent with Hart and Zingales' claim. In other words, when I say that corporate interest need not be equated with shareholders' interests, I understand the latter to refer to the maximisation of share price. But where shareholders' interests are defined to mean the long-term value and viability of the company, there is no contradiction between promoting shareholders' interests and corporate interest.

B. Objective or subjective

There are two key issues relating to the controlling shareholders' duty to act in good faith in the best interests of the company. The first concerns what the company's interests are. This issue has been critically and extensively analysed from a legal, empirical and normative perspective. The second issue is whether a subjective test, objective test or a combination of both applies to this duty, to which I now turn. This issue has been analysed in the case law and academic literature on the duty of directors to act in good faith in the best interests of the company. Regard should be paid to them in interpreting and applying the fiduciary duty that I argue should be imposed on controlling shareholders.

Under UK[127] law and the laws of Singapore[128], Hong Kong[129], Malaysia[130] and India[131], fiduciary duty requires directors to honestly believe that they are acting in the company's best interests. This is the subjective part of the test. Under English law and the laws of Singapore, Hong Kong and India, if directors honestly believe that they have acted in the company's best interests, their decision will not be set aside unless it is one that no reasonable director could

[127] *Re Smith & Fawcett* [1942] Ch 304; *Regentcrest plc v Cohen* [2001] 2 BCLC 80.

[128] *Ho Kang Peng v Scintronix Corp Ltd* [2014] 3 SLR 329 [37].

[129] *Akai Holdings Ltd v Kasikorn Bank Pcl* [2010] 3 HKC 153 (CA); *Thanakharn Kasikorn Thai Chamkat (Mahachon) v Akai Holdings Ltd* (2010) 13 HKCFAR 479.

[130] s 213(1), MY CA; *Pioneer Haven Sdn Bhd v Ho Hup Construction Co Bhd* [2012] 3 MLJ 616.

[131] S 166(2) India Companies Act 2013. It is not clear whether under s 166(2), "good faith" only applies to the duty to "promote the objects of the company" or it also applies to "the best interests of the company". Nothing in the parliamentary materials suggests the former interpretation. The latter interpretation will be consistent with Indian cases prior to the enactment of the Act which affirm that directors have to act in good faith in the company's best interests: see eg, *M/s. Needle Industries (India) Ltd. v. Needle Industries Newey (India) Holding Ltd.* [1981] 3 SCC 333 1981 Indlaw SC 403 at [125]. *Dale and Carrington Invt. P Ltd v P.K. Prathapan* AIR 2005 SC 1624.

have ever arrived at.[132] This is the objective part of the test. But note that this objective aspect does not allow courts to set aside the directors' decision because they take the view that it is unreasonable. The standard is not unreasonableness, rather it is irrationality. As long as the decision, from the standpoint of a reasonable director, is not irrational, courts are unlikely to invalidate the director's decision.[133] There is another objective part of the test: courts will examine the truthfulness of the directors' assertions that they have acted in the company's interests by examining whether there is evidence to support such an assertion.[134] If the evidence is lacking or if the assertion is contradicted by the evidence, the decision is likely to be set aside. But the court will not set aside the decision because it is not commercially justified.

However, the objective test under Malaysian law is different from that under English law and the laws of the other three Asian jurisdictions. The standard is not rationality; rather, it is reasonableness: what would a reasonable director have done, not whether it is something that no reasonable director could have ever done. Under Malaysian law, if the board honestly believes that it has acted in the company's best interests, its decisions will not be set aside if in the totality of the existing circumstances, a reasonable board could have believed that the decision was in the company's best interests.[135] When Malaysian courts applied this objective test, they stated that they are applying the *Charterbridge* test, namely, 'whether an intelligent

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[132] *Regentcrest v Cohen* [2001] BCLC 80 [120]; Hans Tjio and others, *Corporate Law* (Academy Publishing 2015) [09.043]; *Pioneer Haven Sdn Bhd v Ho Hup Construction Co Bhd* [2012] 3 MLJ 616 [238]; Lo and Qu (n 76) [8.043]; *Starlite Spintech Limited v Dijaya-malind Properties (India) Private Limited* C.P.No. 81of 2011 (TP.No. 60/HDB/2016) [27]. It is trite law that bona fides alone is insufficient. In the oft-quoted passage by Bowen LJ from *Hutton v West Cork Railway Co* (1883) 23 Ch. D. 654, 671, '[b]ona fides cannot be the sole test, otherwise you might have a lunatic conducting the affairs of the company, and paying away its money with both hands in a manner perfectly bona fide yet perfectly irrational.'

[133] *Regentcrest v Cohen* [2001] BCLC 80; Hans Tjio and others *Corporate Law* (Academy Publishing 2015) [09.043]; Lo and Qu (n 76) [8.043].

[134] *Regentcrest v Cohen* [2001] BCLC 80.

[135] *Pioneer Haven Sdn Bhd v Ho Hup Construction Co Bhd* [2012] 3 MLJ 616; *Petra Perdana Bhd v Tengku Dato Ibrahim Petra* [2014] 11 MLJ 1; Aiman Nariman Mohd Sulaiman and Effendy Othman, Malaysia *Company Law: Principles and Practices* (Wolters Kluwer 2015) [10.033]-[10.035].

and honest man in the position of the director of the company in question, could in the totality of the circumstances have reasonably believed that the transaction was for the company's benefit.'[136]

However, the courts in the UK[137], Singapore[138] and Hong Kong[139] apply the *Charterbridge* test differently from the Malaysian courts. They apply it only if the directors did not even consider the company's interests. But if the directors have considered the company's best interests, the UK, Singapore and Hong Kong courts do not apply the *Charterbridge* test and instead apply the rationality standard. To apply the *Charterbridge* test to the situation when directors have not even considered the company's interests has been criticised for undermining the duty by not only downplaying the importance of giving consideration to the company's interests, but also 'rewarding' directors who have failed to give any consideration at all. It has been said that directors ought to be held liable for breaching the duty if they fail to give any consideration but if the transaction was nevertheless objectively in the company's best interests, then no consequences would arise from the breach.[140] Indian case law seems to have neither endorsed nor rejected the *Charterbridge* test.

Thus, while the courts in the five jurisdictions subscribe to a combination of subjective and objective tests, important differences lie with respect to the standard applied in the objective test (i.e. rationality in UK, Singapore, Hong Kong and India but reasonableness in

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[136] *Charterbridge Corporation Ltd v Lloyds Bank Ltd* [1970] Ch 62.

[137] Ibid.

[138] *Ho Kang Peng v Scintronix Corp Ltd* [2014] 3 SLR 329.

[139] *Akai Holdings Ltd v Kasikorn Bank Pcl* [2010] 3 HKC 153.

[140] See Rosemary T Langford and Ian M Ramsay, 'Directors' Duty to Act in the Interests of the Company – Subjective or Objective' [2015] *Journal of Business Law* 173, 180. The important thing is that the approach taken with respect to controlling shareholders' fiduciary duty to act in the company's best interest should be consistent with that taken in relation to directors' duty. The law will be incoherent if the *Charterbridge* test is applied in the context of directors' duties, but in view of the criticisms, rejected in the context of controlling shareholders' duties.

Malaysia) and the circumstances under which the *Charterbridge* test will be applied (i.e. only when directors have not considered the company's interests (as in the UK, Singapore and Hong Kong) or when directors have considered them (as in Malaysia)).

It is suggested that a combination of both subjective and objective elements in the test for determining directorial breaches should be applied to determine whether controlling shareholders have acted in good faith in the company's best interests. This is because the combination of both subjective and objective elements in the test will ensure that due regard is paid to the decisions of the controlling shareholder, and that they will not be easily set aside simply because a disgruntled shareholder disagrees with the decision, while ensuring that controlling shareholders are appropriately held accountable for their decisions.

As for whether the standard in the objective test should be rationality (as in the case in the UK, Singapore, Hong Kong and India) or reasonableness (as in the case in Malaysia), and as for the circumstance in which the *Charterbridge* test should be applied (i.e. only when directors have not considered the company's interests as in the case in the UK, Singapore and Hong Kong or when directors have considered the company's interests as in the case in Malaysia), the important point is that there should be consistency in the approach taken with respect to directors' duties and controller's duties. This is to ensure coherence in the law.

It is suggested that the correct approach for both directors and controllers' best interest duty ought to be this: adopt a combination of the subjective and objective test, but the standard for the latter should be rationality and not reasonableness, following the approach in UK, Singapore, Hong Kong and India. When fiduciaries have not even considered the company's best interests, they will be in breach of their duties, and the *Charterbridge* test should not be applied, contrary to the approach in the UK, Singapore and Hong Kong.

In addition to the issue of the subjective/objective elements of the duty, the best interest duty may also require disclosure of any action on the part of fiduciaries that may harm the company's interests.[141] The duty may also require disclosure of wrongdoing.[142] Further, the best interest duty may encompass the duty to exercise independent judgement and to retain, and not fetter, discretionary power.[143]

II. Duty to avoid unauthorised conflict of interest and unauthorised receipt of profits

The no-conflict and no-profit rule helps fiduciaries to fulfil their duty to act in good faith in the best interests of the company because compliance with the no-conflict rule and no-profit rule will make it less likely that fiduciaries will breach the best interest duty.[144] The no-conflict and no-profit rule as applied to fiduciaries requires them not to put themselves in a position where there is an actual or potential conflict of interest (with the latter understood as a real sensible possibility of conflict and not just any imaginary or hypothetical conflict[145]). Should they be in such a position, they will be in breach of the no-conflict rule, unless authorisation is sought from the company, or unless the company ratifies the transaction (but

[141] *Fitzsimmons v The Queen* (1997) 23 ACSR 355, 363-4; Lo and Qu (n 76) [8.029].

[142] *Item Software (UK) Ltd v Fassihi* [2005] 2 BCLC 91; *GHLM Trading Ltd v Maroo* [2012] EWHC 61; *Shepherds Investments Ltd v Walters* [2007] 2 BCLC 202.

[143] Alan J Dignam and John Lowry, *Company Law* (8th edn, Oxford 2014) 356 [14.42]. This does not imply that shareholders cannot contractually bind themselves to vote in certain ways. Directors can contract to vote in certain ways but that does not amount to an impermissible fettering of discretion if the directors can show that, at the time that they enter into contracts to vote in a certain manner, it was in the company's best interests: *Thorby v Goldberg* (1964) 112 CLR 597. By analogy, shareholders' agreement which requires shareholders to vote in a certain manner should not contravene the controlling shareholder's duty to act in good faith in the company's best interests if the controller has considered that doing so is in the company's best interests.

[144] *Chan v Zacharia* [1984] 154 CLR 178, 198-199; *Bray v Ford* [1896] AC 44, 51-52.

[145] *Boardman v Phipps* [1967] 2 AC 46, 124.

not all transactions are always ratifiable).[146] And should fiduciaries also breach the no-profit rule, they will be required to disgorge the profits, whether or not the company is willing or able to pursue the transaction.[147] These general principles governing the no-conflict and no-profit rule as applied to directors should also apply to controlling shareholders.

However, the no-conflict and no-profit rule only prohibits unauthorised conflicts and unauthorised receipt of profits. Thus, an important question is whether there are authorisation mechanisms. There is no statutory mechanism in the four common law jurisdictions in Asia to authorise conflicts of interest involving directors. The UK, however, has one. Under s 175(4)(b) of the UK Companies Act 2006, directors' duty to avoid conflict of interest is not infringed if the matter has been authorised by the board. Under s 175(5)(b), the board can authorise the matter provided that the public company's constitution has a provision that enables the directors to do so in accordance with the constitution. Under s 175(6), the interested director cannot be part of the quorum and she cannot vote. Under the UK Companies Act, authorisation only applies with regards to the avoidance of the no-conflict rule (into which is subsumed the no-profit rule), not to the duty to promote the success of the company (which is based on the common law duty to act in good faith in the company's best interests).

It is suggested that the UK statutory mechanism for authorising conflicts of interest involving directors can be adopted with modification by the four common law Asian jurisdictions for the purpose of authorising conflicts of interest involving controlling shareholders.[148] Given that it is not the director but the controlling shareholder who is seeking

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[146] *Regal (Hastings) Ltd v Gulliver* [1967] 2 AC 134n, 150.

[147] *Bray v Ford* [1896] AC 44, 51.

[148] Another suggested solution is that authorisation has to be provided by both an independent board of directors and disinterested shareholders. The problems associated with independent directors, particularly the fact that they will be pressurised not to defy the wishes of the controlling shareholder because he has the power to dismiss or reappoint them, will be addressed below in n 150 and accompanying text.

authorisation, the notion of the 'interested director' under the UK Companies Act does not apply. Rather, the concern is that directors who are responsible for deciding whether to give the authorisation consist of, or are connected to, the controlling shareholder. In other words, the directors are not disinterested. For example, the director is also the controlling shareholder, or the director is a nominee of, or connected[149] to, the controlling shareholder. The suggested modification to the UK statutory mechanism is that any director who is the controlling shareholder himself, or any director who is a nominee of, or connected to, the controlling shareholder, cannot be part of the quorum and cannot vote to authorise the conflict of interest.

One concern, however, is that even if the director is neither a nominee of, nor connected to the controlling shareholder, he may be subject to pressure to authorise a conflict of interest involving the controlling shareholder. This is because the controller has the power to reappoint or dismiss him.

This concern can be addressed because the controlling shareholder is subject to the duty to act in good faith in the company's best interests when he exercises corporate power through voting or informal power through influence with respect to corporate actions, which include but are not limited to the appointment and dismissal of directors.[150] After all, although a company can authorise conflict of interest or vary the consequences arising from a breach of

[149] By 'connected', it means (a) the director is a family member or employee of the controlling shareholder; (b) the director is a trustee of any trust in which the either the controlling shareholder, or the latter's family member, is a beneficiary; (c) the director is also a director of another company in which the controlling shareholder seeking authorisation is a controlling shareholder; (d) the director has a material business relationship, or has a material interest in a business dealing, with the controlling shareholder; or (e) the director is in a partnership with either the controlling shareholder or the latter's family member, and partnership is defined under the respective jurisdiction's partnership legislation. The definition of connected here is adapted from the definition of connected in Hong Kong Companies Ordinance, s 486; MY CA, s 197; and Singapore Companies Act (Cap 50), s 25D.

[150] The circumstances under which controlling shareholders should be subject to fiduciary duties are elaborated in chapter 5.

the no-conflict rule, it is highly doubtful that a breach of the best interest duty can be authorised.[151]

So, for example, the controlling shareholder wishes to pursue a corporate opportunity and makes a full and frank disclosure to, and seeks authorisation from, the directors who are neither nominees of, nor connected to, the controlling shareholder. The controlling shareholder could be in breach of his duty to act in the company's best interests, if: (a) he exerts influence on the directors to pressurise them to authorise the transaction; (b) he dismisses the directors after they refuse to give the authorisation; or (c) he dismisses the directors before they make the decision knowing that they are likely to oppose the transaction and he appoints directors who will approve the transaction.[152] Another example is that where a controlling shareholder of Company A seeks to acquire shares in Company B (which is or is likely to be a competitor of Company A), he has to make full and frank disclosure and seek authorisation from the directors of both Company A and Company B. If the controlling shareholder were to exert any influence on the directors of either company to give the authorisation, he could be in breach of his duty to act in the best interests of both companies.

To conclude, in this chapter, I have critically analysed the contents of the two fiduciary duties that should be imposed on controlling shareholders of the listed companies of the four Asian common law jurisdictions, namely, the duty to act in good faith in the best interests of the company, and the duty to avoid unauthorised conflict of interest and unauthorised receipt of profits. With respect to the best interest duty, I argued that corporate interest can refer to the long-term value and viability of the company, whose interests are distinct from, and need not

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[151] See eg, *Madoff Securities International Ltd. v Raven* [2013] EWHC 3102 (Comm.) [123]; *Armitage v Nurse* [1997] Ch 241; *Forge v Australian Securities and Investments Commission* [2004] NSWCA 448; (2004) 213 ALR 574 [238].

[152] Questions concerning on how breaches can be enforced will be examined in the chapter on enforcement (Chapter 6).

be reduced to, those of its shareholders and other stakeholders. To support this argument, I critiqued two conventional theories and drew on three theories. This is followed by a critical analysis of the laws of the four Asian jurisdictions, the conclusion of which is that with the exception of Hong Kong, the laws of the other three Asian jurisdictions are consistent with my argument. Finally, I conducted an empirical analysis of the avowed corporate purposes of the top 30 listed companies, the most important finding of which is that a significant percentage of these companies have purposes that underscore the importance of the corporate entity. Having analysed what corporate interest means, I examined the issue of whether an objective test, subjective test or combination of both tests should apply to the best interest duty, and I concluded in favour of a combination test. Finally, I analysed the second fiduciary duty, i.e. the no-conflict and no-profit rule and I argued that all four Asian jurisdictions should adopt a mechanism in which disinterested directors should be allowed to authorise conflicts of interest involving the controlling shareholder.

DPHIL CHAPTER 5: THE MECHANICS OF IMPOSING DUTIES: 'WHEN', 'WHO' and 'HOW'

I. When should the fiduciary duties be imposed?
   A. When does a fiduciary relationship arise?
   B. Exercise of corporate powers by controlling shareholders
   C. Exercise of influence by controlling shareholders
   D. Other situations

II. Who should impose the fiduciary duties?
   A. Legislature
   B. Courts
   C. Stock Exchange

III. How can the fiduciary duties be imposed?
   A. Legislature
      1. Opting-out
      2. Managing liabilities
   B. Courts
      1. Fiduciary relationship
      2. Legitimate expectation
      3. Consensual undertaking
   C. Stock exchange

In the previous chapter, I explained the contents of fiduciary duties. In this chapter, I will explain the mechanics of imposing the duties, which consist of three issues, namely, when the fiduciary duties should be imposed, by whom should the fiduciary duties be imposed, and how the duties can be imposed.

Regarding the first issue, I argue that fiduciary duties should be imposed on controlling shareholders when they exercise corporate powers; when they exert influence on the company and but for the influence, the company would not have made the decision that benefited the controller but at the company's expense; and when there is a conflict of interest between the controlling shareholder and the company which gives rise to extractions of private benefits of control.

Regarding the second issue, I conduct a cost-benefit analysis of whether the legislature, courts or stock exchange should impose the duties. I argue that there is no conclusive answer given that there are advantages and disadvantages associated with each of these institutions and in light of the different contextual considerations in each of the four jurisdictions.

Finally, I examine the third issue, i.e. how the duties could be imposed by the legislature, courts and stock exchange. In relation to the legislature, I argue that it can impose the duties via two routes, the first of which is to impose a default rule that subjects controllers to fiduciary duties but allowing them to opt-out from this rule; and the second is to impose a mandatory rule but having a basket of mechanisms to ameliorate the consequences of the breach of the rule. With respect to the courts, I argue that they can impose the duties using two approaches, the first of which is to hold the controlling shareholder liable as a shadow or de facto director, and the second is to impose the duties depending on whether the facts warrant such an imposition. Finally, as for the stock exchange, I argue that it can adopt a dual-regulatory regime, under which companies can choose whether or not to be subject to the fiduciary duties.

I. When should the fiduciary duties be imposed?

A. When does a fiduciary relationship arise?

As to when fiduciary duties should be imposed, it would depend on when a fiduciary relationship arises.[1] A fiduciary relationship arises when 'one party (the fiduciary) exercises

[1] For a good analysis of the debate, see Paul B Miller, 'The Fiduciary Relationship' in Andrew S Gold and Paul B Miller (eds), *Philosophical Foundations of Fiduciary Law* (OUP 2014) 64-90; Paul B Miller, 'A Theory of Fiduciary Liability' (2011) 56 *McGill Law Journal* 235. There are two views of when a fiduciary relationship arises: one is the status-based approach (i.e. whether the relationship falls within established categories) and the other is the fact-based approach (i.e. whether the indicia of a fiduciary relationship are present in the facts). Miller criticises both approaches and advances a third approach which is a refinement of the fact-based

discretionary power over the significant practical interests of another (the beneficiary).'[2] But having discretionary power that affects the interests of the other, in itself, is insufficient to characterise it as fiduciary. After all, the self-interested exercise of an option in a contract (such as to purchase property or shares) is not considered a fiduciary power. Fiduciary power can be distinguished from such power because the fiduciary's power is derived from the legal personality of the beneficiary and the power is a 'substitutive exercise of legal capacity.'[3] The fiduciary is authorised to act on behalf of the beneficiary and its decision changes the legal position of the beneficiary. Practical interest refers to the welfare and the rights of the beneficiary.[4] Welfare refers to financial and non-financial well-being. Rights refer to the exercise, performance, enforcement and discharge of legal rights, powers and obligations.

There are also three other aspects of the fiduciary relationship: inequality, dependence, and vulnerability.[5] There is inequality because the fiduciary possesses and exercises discretionary power over the beneficiary, thus the relationship will be unequal in relation to the possession and exercise of the power. There is dependence because the beneficiary depends on the fiduciary to obtain certain results or to fulfil certain purposes. There is vulnerability because the interests of the beneficiary could be adversely affected by the exercise of power by the fiduciary. It has been said that discretion, power, inequality, dependence and vulnerability

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approach, i.e. there are necessary and distinguishing features of a fiduciary relationship. The fact-based approach does not come up with the essential features of a relationship.

[2] Paul B Miller, 'The Fiduciary Relationship' in Gold and Miller (n 1) 69; Paul B Miller, 'A Theory of Fiduciary Liability' (2011) 56 *McGill Law Journal* 235.

[3] Paul B Miller, 'The Fiduciary Relationship' in Gold and Miller (n 1) 71.

[4] Ibid at 73.

[5] See eg, *Frame v Smith* [1987] 2 SCR 99, 136; *Hospital Products Ltd v United States Surgical Corporation* (1984) 156 CLR 41, 142; Paul B Miller, 'The Fiduciary Relationship' in Gold and Miller (n 1) 73.

evidence a relationship whereby one party has a legitimate expectation that the other party will act in the interests of the former.[6]

It has been said, however, that dependency and vulnerability are insufficient in themselves to impose fiduciary duties. Another important element of the fiduciary relationship is that it is difficult and costly to monitor the exercise of discretionary power by the fiduciary[7] especially in view of the information asymmetry between the fiduciary and beneficiary.[8]

The above understanding of when fiduciary duties arise – one party (the fiduciary) exercises discretionary power over the significant practical interests of another (the beneficiary, i.e. the company) and alters the legal position of the beneficiary, and the presence of inequality, dependence and vulnerability – is applicable to controlling shareholders, which will be elaborated below.

B. Exercise of corporate powers by controlling shareholders

As explained in Chapter 3, shareholders are conferred significant and substantial powers by the statute, listing rules and company's constitution. These powers are amplified when the shareholders are also the controllers, as is the case in the four Asian jurisdictions. Further and crucially, when controlling shareholders exercise a number of these powers, their decisions bind the company, alter its legal position, and have an impact on its interests. These

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[6] *Arklow Investments Ltd v Maclean* [2000] 1 WLR 594, 598; UK Law Commission, *Fiduciary Duties of Investment Intermediaries* (Law Com No 350) (1 July 2014) para 3.24; Paul Finn, 'The Fiduciary Principle' in Timothy G Youdan (ed), *Equity, Fiduciaries and Trusts* (Law Book Co 1989) 46.

[7] Joshua Getzler, 'Ascribing and Limiting Fiduciary Obligations' in Gold and Miller (n 1) 43-4.

[8] Amir N Licht, 'Motivation, Information, Negotiation: Why Fiduciary Accountability Cannot be Negotiable' in Andrew Gold and D Gordon Smith (eds), *Research Handbook on Fiduciary Law* (Edward Elgar 2018).

corporate powers include appointing or removing directors; dictating to the directors or overruling their decisions; directing directors to take action or making binding recommendations to directors; exercising management powers; authorising major transactions; or authorising or ratifying breaches of directors' duties.[9] In each of these situations when the controlling shareholder exercises corporate power, inequality, dependence and vulnerability are also present. Further, as examined in Chapter 3, in light of the problems of opportunism, information asymmetry and incomplete contracts, it would be difficult to monitor the exercise of powers by the controlling shareholders. In each of the aforementioned situations in which the controlling shareholders exercise corporate power, fiduciary duties should be imposed on them.

To elaborate, consider four examples of controlling shareholders exercising corporate power over the interests of the company and which bind the latter. In these examples, which are illustrative and not exhaustive, the controller should be subject to fiduciary duties. First, when a controlling shareholder dismisses those directors who recommended the rejection of a value-decreasing RPT (because, for example, they are below market value) and appoints directors who would favour them, the controller's appointment and removal decisions are legally binding on the company and they adversely impact on corporate interest because the RPT is detrimental to the company. Second, when a controlling shareholder directs directors to enter into certain transactions or to take certain action, this decision made by the controller binds the company, and although it may benefit the controller, it may not be in the interests of the company. Third, regarding the approval of major transactions, when a controlling shareholder approves a disposal of the company's assets at below-market value, these assets belong to the company and not to the shareholders; the decision by the controlling shareholder

[9] See Chapter 3.

is legally binding on the company and has an adverse impact on its interests. Finally, when a controlling shareholder authorises a transaction or an act by a director who is an associate or nominee of his (which would otherwise amount to a breach of directors' duties) or when the controller ratifies breaches of duties by directors, the ratification alters the legal position of the company and such ratification may not be in the company's interests. This is because the defaulting director's negligence or breach of the no-conflict and no-profit rule might have resulted in financial losses and reputational damage to the company but the controller has decided to ratify the breach because, for example, the director is his family member.

C. Exercise of influence by controlling shareholders

However, the powers wielded and exercised by controlling shareholders are not restricted to the exercise of corporate power by voting such as when they appoint or remove directors; dictate to the directors or overrule their decisions; direct directors to take action or when they make binding recommendations to directors; exercise management powers; authorise major transactions; and authorise or ratify breaches of directors' duties. They can also exercise informal power by exerting influence or applying pressure on the company, and but for the influence, the company would not have made the decision that benefited the controller but which is at the company's expense. In such situations involving conflict of interest and extraction of private benefits of control, fiduciary duties should be imposed on controlling shareholders. For example, as examined in Chapter 3, the controlling shareholder can put pressure on the board to issue disproportionately large dividends. Further, in view of the existing business relationships between the controller and the company, the controller can exert influence on the directors to take or refrain from taking certain actions that would benefit the controller but which are at the company's expense (see the section 'Category 2: Exercise of powers other than by voting – Existing business relationships with the company').

Moreover, the controller can exert influence in connection with RPTs, which are a pervasive and persistent method through which controlling shareholders extract private benefits of control from the company, as I have explained in Chapter 3. There are four possible situations in which the controlling shareholder can exert influence in relation to RPTs.

First, if a controlling shareholder exerts influence on the committee of independent directors in Hong Kong, or the audit committee in Singapore and Malaysia, and but for the influence of the controller, the committee would not have recommended the approval of the RPT, the controlling shareholder may be in breach of his fiduciary duty if he stands to make a personal gain from the RPT that is at the company's expense. A controlling shareholder could exert influence by threatening to dismiss any director in the committee who defies his wishes; or the controller could tell the director that if he wants to be reappointed, he should not disagree with him.

Second, if a controlling shareholder (or his associate[10]) is a member of the audit committee, and exerts influence on the rest of the members of the audit committee to either recommend in favour of the RPT (as the opinion of the committee is required in Singapore and Malaysia) or to actually approve the RPT (as approval and not merely advice/recommendation is needed in India), and but for the influence of the controlling shareholder, the audit committee would not have recommended or approved the RPT, the controller may be in breach of his fiduciary duty, if he stands to make a personal gain from the RPT that is at the company's expense.[11]

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[10] Associate here refers to the controlling shareholder's family member or a 30%-controlled company held directly or indirectly by the controller and/or his family members: see HKEX LR 14A.12.

Third, where the controlling shareholder (or his associate) is a member of the nominating committee, and exerts influence on the other members to nominate his preferred independent directors, and but for the influence of the controller, the nominating committee would not have appointed that director[12], the controller may be in breach of his fiduciary duty if he stands to make a personal gain at the company's expense.

Fourth and finally, if a controlling shareholder (or his associate) who is also a board member influences the rest of the board members so that they alter the powers or resources of the nominating committee so as to influence the nominating committee to nominate independent directors that are favoured by the controlling shareholder, the latter may be in breach of his duty if he stands to make a personal gain at the company's expense.

Regarding the first situation above, it may be objected that it is unnecessary to impose fiduciary duties on the controlling shareholder as he will be held liable as a shadow or de facto director in this particular situation. However, as discussed in Chapter 3, a one-off direction will not turn a controlling shareholder into a shadow director. It has to be done on a continuing basis; a regular course of conduct has to be demonstrated.[13] Further, exerting influence on the directors to approve an RPT may not rise to the level of assuming the status and functions of a director, which is necessary for establishing that the controlling shareholder is a de facto director. And where the person acts as an employee, adviser or agent of the company or as a shareholder who is concerned about his investment, he will not be treated as a de facto

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[11] Under the rules in Singapore and Malaysia, the audit committee has to consist of a majority of independent directors, and in India, two-thirds of the committee have to consist of independent directors. This allows the controlling shareholder or his associate to be a minority member of the committee.

[12] The nominating committee only has to comprise a majority of independent directors in Hong Kong, Singapore and Malaysia and at least 50% in India, which leaves room for the controlling shareholder or his associate to sit on the nominating committee. HKEX LR, Appendix 14A 5.1; Singapore Code of Corporate Governance 2018, Provision 4.2; Bursa Malaysia LR 15.08A(1); s 178(1) of IN CA 2013.

[13] *Secretary of State for Trade and Industry v Becker* [2003] 1 BCLC 555; *Ultraframe (UK) Ltd v Fielding* [2005] EWHC 1638 [1270]-[1278]; *Re Unisoft Group Ltd (No 3)* [1994] 1 BCLC 609, 620.

director.[14] And where there is doubt as to whether the conduct of the person amounts to an assumption of the office of a director or another capacity, the person will not be regarded as a de facto director.[15]

Regarding the second, third and final situation above, it may be objected that it is unnecessary to subject controlling shareholders to fiduciary duties because the controlling shareholder as a member of the audit committee, nominating committee or board of directors could be in breach of the director's duty to act in good faith in the company's best interests. The rebuttal is that it is unlikely that the board of directors will commence legal proceedings against the controlling shareholder for breach of director's duties because he can dismiss or refuse to re-appoint those directors who oppose him. But it may be said that even if fiduciary duties were imposed on the controlling shareholder, the board is also not likely to sue the controller for fear of being removed by the controller. The difference is that where controlling shareholders are subject to fiduciary duties, the actual or threatened removal in this context may constitute a breach of the controller's fiduciary duties. This should increase the board's incentive to sue the delinquent controller. By contrast, where a controlling shareholder is not subject to fiduciary duties when he exercises his power to remove (or appoint directors), the board will be disincentivised to sue the controller.

Further, where the board does not take action against the delinquent director (who is also the controlling shareholder), it is unlikely that a minority shareholder will be permitted to pursue a derivative action for the breach of director's duties by the controller because the RPT is subject to minority shareholders' approval. In other words, in the second situation described above, even if the audit committee (in Singapore or Malaysia) recommends in favour of the

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[14] *Secretary of State for Trade and Industry v Hollier* [2007] BCC 11.

[15] *Re Richborough Furniture Ltd* [1996] 1 BCLC 507, 524; *Re Mumtaz Properties Ltd, Wetton v Ahmedi* [2012] 2 BCLC 9 [30]; *Re UKLI Ltd, Secretary of State for Business, Innovation and Skills v Chohan* [2013] EWHC 680 [38].

RPT because of the influence exerted by the controlling shareholder who sits as a non-independent director on the committee, the disinterested shareholders (who will include the aggrieved minority shareholder in question) can vote against the RPT. Even if the minority shareholder is outvoted and the other disinterested shareholders vote in favour of the RPT, it is unlikely that the minority shareholder will succeed in obtaining leave from the court to commence the statutory derivative action as he will not be able to persuade the court that it is in the company's interests to do so. This is because the disinterested shareholders are authorised to make decisions, and a majority of them have made the decision to approve the RPT on the company's behalf.

It might be objected, however, that rather than subjecting controlling shareholders to fiduciary duties, the solution is to reform the rules related to the independent directors, so as to insulate them from the controlling shareholders' interference. Among the voting powers given to shareholders, the power to appoint and dismiss directors is one of the most, if not the most, crucial and potent tools given to them. One possible solution is to change the listing rules such that only disinterested shareholders can appoint, dismiss and reappoint independent directors.[16] However, given the vital and prominent role of independent directors in providing oversight, particularly where there are acute conflicts of interest involving controlling shareholders such as in RPTs, depriving a controlling shareholder of the right to appoint and dismiss independent directors would in effect substantially deprive him of his ability to exercise influence on the company, particularly on matters in which he arguably has the most at stake such as RPTs. Controlling shareholders would be unlikely to be willing to relinquish control, particularly if they hold a significant percentage of the company's shares.[17] Delinking voting rights and cash

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[16] Lucian Bebchuk and Assaf Hamdani, 'Independent Directors and Controlling Shareholders' (2017) 165 *University of Pennsylvania Law Review* 1271.

[17] Behaviourial law and economics tells us that people tend to value things more because they have them than when they do not have them. The result is that people will often demand a higher price to give up or sell what

flow rights, particularly for controlling shareholders in concentrated ownership jurisdictions in matters that directly impinge on their interests, is highly controversial.

Thus, the suggestion that with respect to conflicted decisions, non-controlling shareholders should, at the minimum, be given exclusive power to dismiss and re-appoint independent directors, and ideally, the power to appoint, dismiss and re-appoint them, is questionable.[18] These scholars sought to assuage the concern arising from the controlling shareholder's relinquishment of control by arguing that the disinterested shareholders should only be given the appointment/dismissal rights with respect to decisions where clear conflicts of interest arise.[19] The problem with this argument is twofold. First, controlling shareholders are likely to have the most interests at stake where there exists the greatest conflict of interest, and thus, they would even be less willing to give up the power to appoint, dismiss and re-appoint independent directors. Second, to restrict those rights only to situations where 'clear conflict of interest exists'[20] (the phrase of which is not defined) is under-inclusive: given the significant powers wielded by shareholders (which are amplified in the case of controlling shareholders) in the common law systems in Asia, conflicts of interest are likely to be pervasive and permeate many areas in which shareholders are given the right to vote, but these areas, as I have demonstrated in Chapter 3, are currently not subject to regulation and which can give rise to extractions of private benefits of control. It has also been argued that controlling shareholders do sometimes give minority shareholders board representation, which undermines the objection of loss of control.[21] However, this argument is unpersuasive because first, the

they have than they will pay for the same thing if it is not part of their endowment: see Richard Thaler, 'Toward a Positive Theory of Consumer Choice' (1980) 1 *Journal of Economic Behavior and Organization* 39. The implication is that it would be very difficult for shareholders, particularly controllers, to give up their right to appoint and dismiss independent directors.

[18] Bebchuk and Hamdani (n 16).

[19] Ibid 1312.

[20] Ibid.

power to dismiss and re-appoint these directors still lies with the controlling shareholders; and second, giving certain minority shareholders board representation is the result of a careful and voluntary bargain entered into between the controlling shareholder and the minority shareholders, which suggests that the controlling shareholder regards it as being in his interests in that specific circumstance to cede limited control.

The other problem is that even if this solution is viable, controlling shareholders who give up their right to appoint and dismiss independent directors are likely to want to be compensated with something else in return.[22] What this additional compensation would be remains unknown. It could be in the form of higher dividends that are guaranteed or transferring certain management powers from the board to the controlling shareholders. Whether this is in the company's interests is debatable. Thus, for example, in exchange for dual class share structure, the American Stock Exchange gave shareholders with no or limited voting rights the power to elect at least 25% of the board.[23]

Finally, there could be two unintended consequences of subjecting the appointment and removal of independent directors to disinterested shareholders' approval. First, there could be a reduction in value-enhancing RPTs because independent directors whose appointment and reappointment now depends on disinterested shareholders may take on an excessively cautious approach and disapprove RPTs that do not provide pro-rata gains to all shareholders but are necessary in certain circumstances, one example of which is that a company is suffering from acute cash flow problems and the directors are not able to find another suitable lender on the desired terms at the desired time. The second and less benign consequence is that activist minority shareholders can appoint their preferred independent directors to the board. There is

[21] Ibid 1311.

[22] This is a consequence of the endowment effect (n 17).

[23] See Joel Seligman, 'Equal Protection in Shareholder Voting Rights: The One Common Share, One Vote Controversy' (1986) 54 *George Washington Law Review* 687, 704 n 90.

thus a risk that these independent directors will be afraid of defying the wishes of these activist minority shareholders.

The other possible solution is to give the power to appoint independent directors to both disinterested shareholders, and the shareholders as a whole, the requirement of which has been imposed in the UK on issuers with controlling shareholders in the premium listing.[24] The manifest weakness of this approach is that there could be stalemate or holdout by minority shareholders if the controllers and minorities cannot agree on the candidate.

Another possible solution is to clarify and tighten the definition of independence such that clear and strict conditions are imposed on the circumstances under which a director qualifies to be an independent director. But there are trade-offs to this proposed solution. The clearer and stricter the conditions, the less discretion the board, acting through the nominating committee, would have in assessing the independence of a director, and hence there would be less room for interference by controlling shareholders. But, given the limited pool of independent directors who have the requisite expertise, there is a risk of exacerbating the difficulty of finding suitably qualified independent directors. For instance, a condition that states that a director who is a family member of a controlling shareholder or who is currently holding or used to hold positions in the controlling shareholder (in the past two years) (assuming the controller is the government) would be automatically disqualified as an independent director would mean that about 50% of the directors in the GLCs in Singapore who are presently treated as independent would no longer be regarded as independent.

One final possible solution that is favoured by some scholars is to subject RPTs to approval (as opposed to recommendation) from both a committee of independent directors and disinterested shareholders.[25] But the problem with this solution is that the independent directors

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[24] Financial Conduct Authority, UK Listing Authority LR 9.2.2A, E and F.

are appointed and can be removed without cause by the general meeting which is effectively controlled by the controlling shareholders.

To conclude, the most common and persistent method used by controlling shareholders to extract private benefits of control is to enter into RPTs with the company. However, interference by controlling shareholders is arguably the most serious problem with the listing rules that regulate RPTs. The interference comes in two main forms: the exercise of corporate power of removal or appointment, and the exercise of influence. Imposing fiduciary duties will help to address the problem of the controller: removing or threatening to remove independent directors who oppose the RPTs; exerting influence on the independent directors who are tasked with deciding whether to recommend the approval of RPTs; exerting influence as a member of the audit committee over the rest of the members of the committee to opine in favour of the RPT; and exerting influence as a member of the nominating committee over the rest of the members to nominate the controller's preferred candidate.

D. Other situations

There are other situations in which the controlling shareholder is neither exercising corporate power nor exerting influence on the company, but there are real or potential conflicts of interest between the controlling shareholder and the company which can give rise to extractions of private benefits of control. It is envisaged that there are at least two such

[25] Luca Enriques, 'Related Party Transactions' in Jeffrey Gordon and Wolf-Georg Ringe (eds), *The Oxford Handbook of Corporate Law and Governance* (OUP 2015) 14-15. As mentioned in Chapter 3, opinion and not approval is required from the audit committee in Singapore (and only if it takes a different view from the independent financial adviser) as well as in Malaysia. In Hong Kong, opinion is required from the independent directors' committee.

situations, the first of which is when the shareholder is a controller in two competing companies ('Investments in competing companies'), and when the controller exploits a corporate opportunity, as examined in Chapter 3. The controller should be subject to fiduciary duties in these two situations.

II. Who should impose the fiduciary duties?

Whether the legislature, courts or the stock exchange should impose the fiduciary duties on controlling shareholders is a difficult question for which there is no straightforward and conclusive answer.[26] There are arguments in support of the legislature imposing the duties, and there are also arguments in favour of the courts doing the same. There are also counter-arguments to each of the 'pro-legislature' and pro-judiciary' arguments, thus adding complexities to the evaluation. One suggestion is for the stock exchange to impose the duties, but there are also drawbacks to this suggestion.

A. Legislature

[26] For a good summary of the arguments for and against judicial and legislative law reform, see eg, Andrew Burrows, 'Post-Legislative Scrutiny, Legislative Boundary and the "Elusive" Boundary' in Matthew Dyson and others (eds), *Fifty Years of the Law Commissions: The Dynamics of Law Reform* (Hart 2016) 195-197; Barbara McDonald, 'Law Reform in Private Law: The Role of Statutes in Supplementing or Supplanting the Common Law' in Dyson and others (n 26) 298-301, 305; Lady Hale, 'Fifty Years of the Law Commission: Then, Now and Next' in Dyson and others (n 26) 23-4; Lord Walker, 'Developing the Common Law: How Far is too Far' (2013) 27 *Melbourne University Law Review* 232.

First, courts should not impose duties because they may run the risk of judicial legislation. It may be said that imposing fiduciary duties on controlling shareholders is not an incremental development of existing legal principles to fill a gap in the law; rather, it amounts to overturning well-established legal position in the four countries in common law Asia, and thus only the legislature should impose the duties, so the objection goes. However, there is a general and a specific rebuttal to this objection. The general rebuttal is that where to draw the line between permissible and impermissible judicial law making has not been made clear, the task of which depends on the specificities of each case. Further, if the objection of judicial legislation were compelling, courts would not have decided many important cases in different fields of law.[27] The specific rebuttal is that imposing fiduciary duties on controlling shareholders is supported by legal and policy justifications.

Second, the legislature can fully consider all relevant perspectives, including legal and non-legal ones, and do a careful and thorough cost-benefit analysis which is likely to involve economic expertise and empirical knowledge. By contrast, courts are unlikely to be equipped to conduct such evaluation. This argument seems persuasive but on closer inspection, it suffers from two serious deficiencies. The first deficiency is that while the legislature would have the expertise or certainly more expertise than the courts, the evaluation and decision of the legislature as to whether or not to impose duties would be affected by interest group politics.[28] It would not be surprising that wealthy and powerful families, who are controlling shareholders

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[27] For eg, *Kleinwort Benson Ltd v Lincoln City Council* [1999] 2 AC 349; *FHR European Ventures LLP v Cedar Capital Partners LLC* [2015] AC 250; *Donoghue v Stevenson* [1932] UKHL 100; Sarah Worthington and others (eds), *Revolution and Evolution in Private Law* (Hart 2018).

[28] The resistance of those who hold economic and political power to positive reforms has been analysed in Mancur Olson, *The Rise and Decline of Nations* (Yale University Press 1982); Raghuram G Rajan and Luigi Zingales, 'The Great Reversals: The Politics of Financial Development in the Twentieth Century' (2003) 69 *Journal of Financial Economics* 5. See also Lucian A Bebchuk and Mark J. Roe, '*A Theory of Path Dependence in Corporate Ownership* and Governance' (1999) 52 *Stanford Law Review* 127, 157-160; Lucian A Bebchuk and Zvika Neeman, 'Investor Protection and Interest Group Politics' (2010) 23 *Review of Financial Studies* 1089; Mariana Pargendler, 'State Ownership and Corporate Governance' (2011) 80 *Fordham Law Review* 2917, 2921-2922.

of the majority of the listed companies in the four countries in Asia, would lobby against any law that imposes fiduciary duties on them.[29] The second deficiency is that given that the government is a controlling shareholder in a number of listed companies in the four countries, it is most unlikely that it would initiate the process of considering whether or not to impose fiduciary duties on itself, let alone eventually deciding to pass such a law. Even if it does commence the process, it could thwart the process by delaying it, under-funding it or refusing to pass the law.

Third, given that there will be qualifications and exceptions to the duties, it would be more feasible for legislature to reform the law rather than the judiciary. The qualifications include but are not limited to the fact that the duty applies only to controlling shareholders. However, while courts may not be able to reform the law as extensively and holistically as the legislature, the piecemeal and incremental nature of judicial reform may be preferable to overhauling the law at one go because the latter could produce unintended or unforeseen consequences that may be difficult to address after the legislation has been passed.

Fourth, the legislature rather than the courts should be the entity imposing the duties because whether courts will impose the duties will depend on the willingness and ability of the litigants to bring the relevant claims and where necessary, to pursue and defend appeals; the specific issues that are in dispute; and finally, the willingness of judges to depart from precedents.

Fifth, given that imposing fiduciary duties on controlling shareholders would not be without contention, it is important to give legitimacy to the decision-making process and the actual decision itself through a mechanism that reflects democratic will. This argument has bite if the issue involves controversial social policies and which is likely to divide and polarise

[29] See eg, Lawrence Saez, 'India: From Failed Development State Towards Hybrid Market Capitalisation' in Michael A. Witt and Gordon Redding (eds), *Oxford Handbook of Asian Business Systems* (OUP 2014) 60; Gordon Redding and others, 'Hong Kong: Hybrid Capitalism as Catalyst' in Witt and Gordon (n 29) 40.

society. Such issues normally occur in criminal law, family law or medical law (such as euthanasia, assisted suicide or same-sex marriage). But it is doubtful whether the democratic legitimacy argument has force in relation to company law, particularly for a discrete issue that affects controlling shareholders and not other stakeholders such as creditors and employees.

Finally, the legislature is arguably more efficient than the courts. The legislature, particularly in countries like Singapore and Malaysia which are dominated by a single party[30], can pass laws more quickly. In India, the courts are very inefficient as it has been found that the average length of time from the moment the proceeding is commenced till the time judgement is rendered is about 10 years.[31] There is also a severe backlog of cases in the Indian courts.[32] The counterargument is that the legislature can be subject to delays and obstructions because of filibustering as is often the case in Hong Kong.[33] Moreover, the government in Singapore and Malaysia which effectively controls the legislature can more easily oppose the proposed law that imposes fiduciary duties on them.

B. Courts

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[30] For eg, Cherian George, *Singapore, Incomplete: Reflections on a First World Nation's Arrested Political Development* (Ethos Books 2017); Edmund Terence Gomez and KS Jomo, *Malaysia's Political Economy: Politics, Patronage and Profits* (2nd edn, CUP 1999).

[31] For eg, Bibek Debroy, 'Some Issues in Law Reform in India' in Jean-Jacques Dethier (ed), *Governance, Decentralization, and Reform in China, India and Russia* (Kluwer 2000) 343.

[32] For eg, John Armour and Pryia Lele, 'Law, Finance, and Politics: The Case of India' (2009) 43 *Law and Society Review* 491, 508-9.

[33] For eg, Tony Kwok, 'Why Hong Kong People Should Support Move to End Filibustering in Legislative Council' *South China Morning Post* (1 Dec 2017).

First, in cases where the government has vested interests, or lacks political will or resources, courts should seize the opportunity to develop the law, rather than leaving it up to the legislature to do so. As mentioned above, the government indeed has a strong vested interest given that it is a controlling shareholder in a number of significant listed companies in all the four countries in Asia. This argument has merit but it may be too sanguine. For example, if a minority shareholder were to sue the government who is the controlling shareholder, and seeks to persuade the court to impose fiduciary duties on the government, it is not clear whether the courts in the four countries in Asia will do so. This is partly because the courts (in India and Malaysia) may not be independent[34] and it is not always clear that the government can be sued.[35]

Second, judicial development of the law is more adaptable and responsive to changing values and circumstances than legislation which may result in the ossification of the law.[36] Thus, it would be more appropriate for courts to reform the law and impose the duties. However, this argument seems to rest on a stark dichotomy between legislation and case law; it seems to assume that the common law has no role to play in interpreting, applying and developing the legislative provision. This assumption is highly questionable. First, unless the legislative provision has the effect of freezing the common law, or the development of the common law will undermine the statutory purpose or terms, courts should not be barred from developing the

[34] For eg, in the most recent and comprehensive survey measuring the rule of law based on the experiences and perceptions of the public and experts, it is stated that one of the factors affecting the rule of law are "constraints on government powers", the criterion of which includes but is not limited to whether government powers are effectively limited by the judiciary. Under the category of constraints on government powers, Singapore, Hong Kong, India and Malaysia are ranked 25, 30, 36 and 74, respectively, out of 113 countries: World Justice Project Rule of Law Index 2017–2018 at 10, 32 <https://worldjusticeproject.org/sites/default/files/documents/WJP_ROLI_2017-18_Online-Edition_0.pdf> accessed 1 December 2018.

[35] For eg, the controlling shareholder of the PRC SOEs listed in Hong Kong, which is the PRC State Council, cannot be sued because the common law doctrine of crown immunity subsisted after the handover of Hong Kong to China, and the immunity of the British Crown was transferred to the PRC government, which is the sovereign government of Hong Kong: *Hua Tian Long* (No. 3) [2010] 3 HKC 557.

[36] Rafael La Porta and others, 'The Economic Consequences of Legal Origins' (2008) 46 *Journal of Economic Literature* 285.

law.[37] For example, suppose that the statute makes no mention of whether a bondholder is subject to fiduciary duties. But suppose that the controlling shareholder is also a bondholder. And the bondholder has been exercising the voting power that has been conferred on it as a bondholder to the detriment of the company. The issue before the court is whether the exercise of voting powers by the bondholder should be subject to fiduciary duties.[38] It is submitted that in this situation, the statute should not be interpreted as precluding the courts from developing the common law in order to impose fiduciary duties on the bondholder in that specific situation, if it is warranted. Second, in interpreting and applying the legislation, courts have to rely on the pre-existing common law.[39] For example, if the statutory provision states that controlling shareholders owe fiduciary duties to the company, courts have to examine the pre-existing common law on fiduciary duties in order to give effect to the statutory provision. Third and finally, unless the legislation expressly excludes the present and future common law, it is not ousted.[40] For example, assume that the legislative provision states that the fiduciary duties can only be excluded in three specific circumstances. Assume also that the issue before the courts concerns the validity of a particular circumstance in which fiduciary duties have been excluded but this circumstance does not fall within the three permissible circumstances in the statute. The common law on the exclusion or modification of fiduciary duties should continue to apply in this situation.

Third, courts should impose the duties because even if courts were to make mistakes in the development of the law or leave gaps unfilled, the legislature can step in to rectify these

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[37] Andrew Burrows, 'The Relationship Between Common Law and Statute in the Law of Obligations' (2012) 128 *Law Quarterly Review* 232, 244-248.

[38] Note that bondholders' exercise of powers is subject to restrictions but not fiduciary duties: *Assénagon Asset Management SA v Irish Bank Resolution Corp Ltd* (formerly Anglo Irish Bank Corp Ltd) [2012] EWHC 2090 (Ch).

[39] Burrows (n 37) 234-6.

[40] Ibid 236-240.

mistakes and to fill the lacuna. The problem with this argument is that it assumes that the legislature will be willing and able to do so. But the legislature could have more pressing tasks to handle, it may not have the resources, or it may think that it would be more appropriate or convenient to leave it to the courts to make the necessary changes.

Fourth, as one cannot be certain whether the legislature will reform the law, and if so, when and how, courts should not abdicate their responsibility to develop the law by passing the buck to the legislature. This argument has particular force in the four countries in Asia because the legislatures in those countries have just completed reforming their companies statutes after many years of study and consultation. It is unlikely that the legislature will reopen or relook into the amendment process or initiate a new amendment to the recently enacted companies statute to impose fiduciary duties on controlling shareholders. For example, Hong Kong's new Companies Ordinance came into effect in 2014 since the commencement of the rewriting of the legislation in 2006.[41] Singapore commenced its review of the Companies Act in 2007 and only completed the review in 2014 and amended parts of the statute.[42] India and Malaysia's new Companies Act came into effect in 2013 and 2017, respectively. However, the persuasiveness of the argument that judges should develop the law depends on their willingness and ability to do so. In the context of imposing fiduciary duties on controlling shareholders, a judge may be disinclined to disturb well-established precedent such as the cases that have affirmed the notion that votes are property rights and shareholders can vote as they please. Or a judge may be wary of ruling against a controlling shareholder who is the government. Thus, one cannot predict whether the courts will change the law.

[41] New Companies Ordinance (Chapter 622 – Highlights), Companies Registry, 2014 <https://www.cr.gov.hk/en/companies_ordinance/docs/NewCO_C622_HL_FullVersion-e.pdf> accessed 1 December 2018.

[42] Accounting and Corporate Regulatory Authority, Companies Act Reform <https://www.acra.gov.sg/Legislation/Companies_Act_Reform> accessed 1 December 2018.

Finally, the legislative amendments may either contradict or bring incoherence or uncertainty to the existing common law, the result of which is that it would be difficult for judges to rectify these shortcomings, and thus it would be better for courts to develop the law instead. This is one of the disadvantages of legislative reform. But it does not follow that it would be more appropriate for courts to develop the law. Given the incremental and necessarily piecemeal nature of judicial development of the law, uncertainty and unpredictability is not necessarily mitigated. For example, a court may decide to hold that a controlling shareholder owes fiduciary duties to the company but refuses to decide whether this duty can be contracted out because it has not heard arguments on this issue. Thus, not only will this generate uncertainty, but it will also be costly because there has to be another litigation that raises this specific issue before the courts will be required to make a determination.

In light of the foregoing analysis of whether the legislature or the courts should impose the duties, it is difficult to arrive at a definitive answer as to which entity is better suited to engage in this particular law reform given that each has its own upsides and drawbacks. It has been forcefully argued that the 'default position'[43] should be that with the exception of family law and criminal law, courts should incrementally develop the law 'where there is the possibility of making a desirable change to the law judicially'[44], and 'it is normally an unacceptable denial of justice to refuse to develop the law on the argument that reform is best left to legislature.'[45] The persuasiveness of this statement hinges on the key word 'desirable'. Whether law reform by courts is 'desirable' cannot be answered without a proper engagement with the 'pro-legislature' and 'pro-judiciary' arguments and their criticisms, and to situate the analysis within the context of each of the four countries in Asia.

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[43] Burrows (n 26) 197.

[44] Ibid.

[45] Ibid.

C. Stock Exchange

Another entity that could impose fiduciary duties on controlling shareholders is the stock exchange or a securities regulator. The stock exchange could issue a new listing rule to impose fiduciary duties on the controlling shareholders of the listed companies. Or the securities regulator could subject listed companies to fiduciary duties. The stock exchanges in the case of Hong Kong and Malaysia (the Stock Exchange of Hong Kong and Bursa Malaysia Berhad) and the securities regulators in the case of India and Singapore (Securities and Exchange Board of India and Monetary Authority of Singapore) have played an important role in corporate governance. This is evident in the listing rules, corporate governance codes and securities laws which regulate matters including but not limited to board composition and committees, related party transactions and financial reports.[46]

There are five main advantages of having the stock exchange or securities regulator impose the duties as compared to courts and legislature. First, it should have more resources than courts to consider all the relevant perspectives before deciding to impose the duties. Second, unlike courts, it does not depend on the litigants bringing and arguing the relevant claims in order to issue the listing rule. Third, unlike courts, it will not fall foul of the criticism that it is acting undemocratically by imposing the duties. Fourth, it is likely to pass the

[46] HKEX Ch 3, 14A; SGX LR Ch 9; Bursa Malaysia LR Ch 10 and 15; Singapore Code of Corporate Governance 2018; Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations 2015.

regulation quicker than the legislature.[47] Fifth, it can amend the rules more easily than the legislature should the rules be found not to be working satisfactorily or if gaps in the rules are discovered later. Finally, given that fiduciary duties will be part of the listing rules (or securities regulations), they will apply to all companies, whether they are locally or foreign incorporated, as long as they are listed on the exchange. But if the legislature were to impose the duties, it will do so through the companies statute which will usually only apply to companies incorporated in the jurisdiction of the legislature and not to overseas incorporated companies. This means that companies that are listed on the stock exchange in Singapore, Malaysia and India but which are incorporated overseas (such as the Cayman Islands, Bermuda or the People's Republic of China) will not be subject to fiduciary duties. Hong Kong, however, is different from the other three countries because overseas incorporated companies that are listed on the Hong Kong Stock Exchange are subject to Hong Kong company law (which includes the Hong Kong Companies Ordinance) because the listing rules specifically prescribe for that[48], and the Hong Kong Companies Ordinance specifically allows enforcement actions (including unfair prejudice and derivative action) to be taken against companies that are incorporated outside of Hong Kong but which has a place of business in Hong Kong.[49]

However, there are three drawbacks if the stock exchange or securities regulator were to impose the duties. First, the stock exchange and securities regulator may be subject to pressure from the government not to impose fiduciary duties. In the case of the stock exchange, a government entity is in charge of regulating the stock exchange and overseeing the rules

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[47] For eg, with regards to the role of the SEBI as compared to courts or legislature, see Armour and Lele (n 32) 501, 506, 510-511, 516.

[48] HKEX LR 3.08, 19.01, 19.05(3)(a).

[49] The listing rule (HKEX LR 19.05(3)(a)) requires overseas incorporated companies to have a "register of holders" for the transfer of shares in Hong Kong, which will constitute a place of business in Hong Kong under s 774(1) HK CO. This will result in Hong Kong courts having the jurisdiction to adjudicate on derivative and unfair prejudice actions in relation to these overseas incorporated companies (ss 722(1), 724 and 732 HK CO).

issued by the exchange, as is the case in Singapore,[50] Malaysia[51] and India.[52] (The Stock Exchange of Hong Kong, however, is regulated by the Hong Kong Securities and Futures Commission[53], which is independent of the government.[54]) Second, given that the GLCs/SOEs are substantial shareholders of the stock exchange in India[55] and Malaysia[56], they may exert pressure on the board of the stock exchange not to impose the fiduciary duties. Although the Stock Exchange of Hong Kong (SEHK) is wholly owned by the Hong Kong Exchanges and Clearing Limited in which the government only owns less than 6% shares[57], the government has the right to appoint up to eight directors in SEHK.[58] Thus the Hong Kong government can exercise influence over the board not to impose fiduciary duties. (In Singapore, however, the government is neither a shareholder of the Singapore Exchange[59] (SGX), nor has the right to appoint the board of SGX.) Third and finally, given that the stock exchanges in all the four

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[50] The Singapore Exchange is regulated by the Monetary Authority of Singapore.

[51] Bursa Malaysia is regulated by the Securities Commission of Malaysia.

[52] The two exchanges in India (Bombay Stock Exchange and National Stock Exchange of India) are regulated by the Securities and Exchange Board of India.

[53] Securities and Futures Commission, Who We Regulate <http://www.sfc.hk/web/EN/about-the-sfc/our-role/who-we-regulate.html> accessed 1 December 2018.

[54] Securities and Futures Commission, Our Role <http://www.sfc.hk/web/EN/about-the-sfc/our-role/> accessed 1 December 2018. But note that the Hong Kong Chief Executive appoints the chairperson and commissioners of the SFC.

[55] The Life Insurance Corporation of India and State Bank of India own 12.5% and 10.2% of the shares in the National Stock Exchange of India, respectively: National Stock Exchange of India, 24th Annual Report 2015-6 at 83 <https://www.nseindia.com/global/content/about_us/AnnualReport-2016.pdf> accessed 1 December 2018.

[56] Kumpulan Wang Persaraan and Capital Market Development Fund own 19.7% and 18.7% of the shares in Bursa Malaysia, respectively: "At the Heart of ASEAN's Growth" Annual Report 2016, Bursa Malaysia, at 202 <http://bursa.listedcompany.com/misc/ar2016.pdf> accessed 1 December 2018.

[57] See HKEX 2016 Annual Report 64 <http://www.hkexnews.hk/listedco/listconews/SEHK/2017/0320/LTN20170320225.pdf> accessed 1 December 2018.

[58] SFO, s 77(1), (5).

[59] See Singapore Exchange 2017 Annual Report 161 <http://files.shareholder.com/downloads/ABEA-69RPAC/6108978920x0x954916/7EEB2232-ED6E-49A8-8D81-B6CAE48FBCC2/2017-sgx-annual-report.pdf> accessed 1 December 2018.

countries are commercial, profit-driven entities, they may not wish to impose fiduciary duties as they may fear that doing so may make them less attractive as a listing venue as compared to other stock exchanges that do not impose such duties.[60]

The final drawback mentioned above is arguably the most salient one in light of regulatory competition.[61] There are four responses to this drawback. First, it has been found that effective investor protection laws, particularly those that constrain extractions of private benefits of control, are a strong predictor of successful stock markets and financial development.[62] There is a correlation between higher share price and more stringent regulatory requirements as well as more robust investor protection laws.[63] This is and ought to be one of the key considerations underlying companies' decision as to where they should list. As companies are interested to tap into external funds, they would want to a list on a stock exchange where the share price will be high. For example, after the Securities Exchange Board of India (SEBI) announced significant and substantial mandatory reforms to corporate governance with regards to independent directors, board composition and financial reporting through the introduction of clause 49 into the Listing Agreement, there was positive stock

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[60] For example, the Hong Kong and Singapore stock exchanges have abandoned their longstanding opposition to dual class shares and now permit such listings under certain circumstances. This complete turnaround is driven by regulatory competition.

[61] For a concise summary, see Reinier Kraakman and others, *The Anatomy of Corporate Law: A Comparative and Functional Approach* (3rd edn, OUP 2017) [1.4.3]; Andreas Cahn and David C Donald, *Comparative Company Law: Text and Cases on the Laws Governing Corporations in Germany, the UK and the USA* (CUP 2010) 65-96; Marcel Kahan, 'The State of State Competition for Incorporations' in Jeffrey N Gordon and Wolf-Georg Ringe (eds*), The Oxford Handbook of Corporate Law and Governance* (OUP 2015) Ch 5.

[62] Simeon Djankov and others, 'The Law and Economics of Self-Dealing' (2008) 88 *Journal of Financial Economics* 430, 461; Nicola Cetorelli and Stavros Peristiani, 'Prestigious Stock Exchanges: A Network Analysis of International Financial Centers' (2013) 37 *Journal of Banking & Finance* 1543, 1550.

[63] Khaled Amira and Mark L Muzere, 'Competition Among Stock Exchanges for Equity' (2011) 35 *Journal of Banking and Finance* 2355, 2363, 2369; Andrei Shleifer and Daniel Wolfenzon, 'Investor Protection and Equity Markets' (2002) 66 *Journal of Financial Economics* 3; John C Coffee, 'Racing Towards the Top: The Impact of Cross-Listing and Stock Market Competition on International Corporate Governance' (2002) 102 *Columbia Law Review* 1757; Yan-Leung Cheung and others, 'Do Investors Really Value Corporate Governance? Evidence from the Hong Kong Market' (2007) 18 *Journal of International Financial Management & Accounting* 86.

market reaction and increase in share price of companies.[64] Further, there is also evidence that to attract listings, stock exchanges have issued stricter rules and have become more aggressive in monitoring listed companies.[65] This seems to cast doubt on the claim that to attract more listings, stock exchange should not have stricter rules to improve corporate governance.

Second, the higher share price could compensate controlling shareholders for their diminished private benefits of control (as a result of the imposition of fiduciary duties).[66]

Third, the department in the stock exchange that is responsible for formulating, developing, issuing and enforcing the listing rules should be independent of the commercial arm of the stock exchange. For example, in Singapore, the entity in charge of the regulatory functions of the Singapore Exchange (SGX) - Singapore Exchange Regulation Pte Ltd (RegCo) - is independent of the commercial arm of SGX.[67] A majority of the directors including the chairman of the RegCo must be independent of SGX. And RegCo is accountable and reports to the Monetary Authority of Singapore (MAS), the regulator in charge of capital market. One problem, however, is that because RegCo is a subsidiary of SGX, the latter retains the power to appoint and dismiss the directors of RegCo. To ensure the independence of RegCo, it is essential that the power of appointment and dismissal lies with the MAS. Singapore's example partially assuages the concern arising from conflicts of interest. This will consequently address

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[64] Bernard S Black and Vikramaditya S Khanna, 'Can Corporate Governance Reforms Increase Firm Market Values? Event Study Evidence from India' (2007) 4 *Journal of Empirical Legal Studies* 749; Dhammika Dharmapala and Vikramaditya Khanna, 'Corporate Governance, Enforcement, and Firm Value: Evidence from India' University of Michigan Law & Economics Olin Working Paper No. 08-005 (2008).

[65] See for example, the stricter regulatory strategy adopted by Shenzhen Stock Exchange in order to attract more listings as compared to its rival the Shanghai Stock Exchange: Benjamin L Liebman and Curtis J Milhaupt, 'Reputational Sanctions in China's Securities Market' (2008) 108 *Columbia Law Review* 929, 958, 978.

[66] Khaled Amira and Mark L Muzere, 'Competition Among Stock Exchanges for Equity' (2011) 35 *Journal of Banking and Finance* 2355, 2363, 2369.

[67] Yeow Eng Goh, 'Making SGX RegCo "Truly Independent"' *Straits Times* (14 Aug 2017).

in part the criticism that the stock exchange is unlikely to impose fiduciary duties because of commercial considerations.

Finally, the claim that the stock exchange's aim to attract as many listings as possible in order to maximise profits, and hence will not impose fiduciary duties on controlling shareholders, does not take into account the fact that companies are motivated by different considerations as to where to list (and cross-list). These considerations[68] include gaining access to new investors[69]; increased visibility[70]; trading shares in more efficient markets; greater access to funds; the types of companies that the stock exchange attract; and importantly, subjecting themselves to more stringent regulatory standards in order to improve their corporate governance so as to signal their commitment to protect outside investors.[71]

In brief, in evaluating the soundness of the claim that regulatory competition militates against the stock exchange imposing fiduciary duties on controlling shareholders, regard should be had to the impact of competition on exchanges' listing rules; the impact of exchanges' listing rules on share price; the reasons underlying companies' decision as to which exchange to list on; the benefits and costs to the shareholders; and the purpose of the listing rules. There is no straightforward answer given that multiple and competing considerations have to be taken into account. An appropriate balance has to be struck between protecting companies by

[68] Marco Pagano and others, 'The Geography of Equity Listing: Why Do Companies List Abroad?' (2002) 57 *Journal of Finance* 2651, 2653-2659.

[69] Robert C Merton, 'A Simple Model of Capital Market Equilibrium with Incomplete Information' (1987) 42 *Journal of Finance* 483.

[70] H Kent Baker and others, 'International Cross-Listing and Visibility' (2002) 37 *Journal of Financial and Quantitative Analysis* 495.

[71] John C Coffee, 'The Future as History: The Prospects for a Global Convergence in Corporate Governance and its Implications' (1999) 93 *Northwestern University Law Review* 641; Edward Rock, 'Securities Regulation as Lobster Trap: A Credible Commitment Theory of Mandatory Disclosure' (2002) 23 *Cardozo Law Review* 675; Craig G Doidge and others, 'Why Are Foreign Firms Listed in the US Worth More?' (2004) 71 *Journal of Financial Economics* 205.

improving its corporate governance (which will benefit investors), allowing companies to raise funds, and maintaining a competitive stock exchange.[72]

D. How can the fiduciary duties be imposed?

A. Legislature

Any legislative law reform that seeks to impose fiduciary duties has to address two major concerns. The first relates to opposition from the controlling shareholders comprising families and particularly the government.[73] The second concern is that the law will disincentivise companies from incorporating in Singapore, Malaysia and India because companies incorporated in those three jurisdictions will be subject to the local statutory company law (and hence the fiduciary duties), as previously mentioned.[74]

[72] To give an example: in deciding whether to list an SOE, and on which stock exchange to list, the PRC government has to balance and weigh multiple and competing considerations such as the need to: raise funds from investors, improve the corporate governance of SOEs by subjecting them to the rigorous SEHK listing rules, and support the economy of Hong Kong vis-à-vis that of mainland China. No single factor is decisive although the need to raise the corporate governance standards of SOEs was and remains a central consideration. See David C Donald and others, *A Financial Centre for Two Empires: Hong Kong's Corporate, Securities and Tax Laws in its Transition from Britain to China* (CUP 2014) 241-246.

[73] (n 28-29).

[74] By contrast, companies that are not incorporated in Hong Kong but which are listed on the Stock Exchange of Hong Kong will still be subject to the Hong Kong Companies Ordinance if it has a place of business in Hong Kong (n 48-49).

Before we discuss the strategies to address these concerns, the second concern should not be exaggerated. In which jurisdiction a company chooses to remain incorporated, and in which jurisdiction a company chooses to incorporate, involve multiple and competing considerations such as tax benefits, politics, rule of law, regulatory requirements, business needs, etc. The substance of company law is just one factor among many others. Even if a jurisdiction has a stringent company law regime (such as having a mandatory law that imposes fiduciary duties on controlling shareholders), it could be 'offset' by other advantages which are more important considerations including but not limited to: tax benefits, high quality of infrastructure services, transparency of public sector procurement, stable macroeconomic conditions, and effective protection and enforcement of property and contractual rights.[75] Thus, on a cost-benefit analysis, businesses may still find it better to incorporate in a jurisdiction with stringent company law, if the conditions for doing business there are favourable. In short, the cost of incorporation is merely one of the many relevant considerations that a company has to take into account but it is not the primary or overriding one.

That said, there are two possible strategies to reduce opposition from the controlling shareholders and to reduce the unattractiveness of the jurisdictions as places of incorporation. The first strategy is to impose fiduciary duties, but it is a default law that can be opted-out. The second strategy is to impose a mandatory law but to have a basket of mechanisms to ameliorate the consequences arising from breach of fiduciary duties (which would include ratification, insurance, indemnities, and application to court for relief).

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[75] World Bank, Doing Business 2018: Reforming to Create Jobs (Comparing Business Regulation for Domestic Firms in 190 Economies) <http://www.doingbusiness.org/~/media/WBG/DoingBusiness/Documents/Annual-Reports/English/DB2018-Full-Report.pdf> accessed 1 December 2018.

1. Opting-out

A legislature can introduce a default law under which fiduciary duties are imposed but the controlling shareholders are given the option to opt-out from the duties. Opting-out here means that the controlling shareholders are seeking complete exemption from fiduciary duties. This opt-out is different from seeking authorisation for a specific matter so that the controlling shareholder in question will not be in breach of its fiduciary duties – this has been examined earlier in Chapter 4 regarding the proposed mechanism for controlling shareholders to seek authorisation from the board so that they will not infringe the no-conflict and no-profit rule. In the latter situation, fiduciary duties are mandatory but controlling shareholders are permitted to obtain authorisation for certain specific acts such that they will not infringe the duty if they carry out those acts. By contrast, in the situation of opt-out, fiduciary duties are not mandatory. The default position is that controlling shareholders are subject to fiduciary duties but these duties can be opted-out provided that certain procedures are complied with.

Opting-out from the law raises the broader and widely debated issue of whether the law should be mandatory or enabling.[76] In determining whether fiduciary duties should be mandatory or enabling, it is critical that the party which the law seeks to protect can give independent and fully informed consent.[77] Given that the beneficiary of the best interest duty and the no-conflict rule is the company, only the company can consent. Should the controlling

[76] See the papers in the symposium edition entitled *'Contractual Freedom and Corporate Law*' (1989) 89 *Columbia Law Review* 1395-774; Anthony Duggan, 'Contracts, Fiduciaries and the Primacy of the Deal' in Elise Bant and Matthew Harding (eds) *Exploring Private Law* (CUP 2010) 278-282; Henry N Butler and Larry E Ribstein, 'Opting Out of Fiduciary Duties: A Response to the Anti-Contractarians' (1990) 65 *Washington Law Review* 1. Cf Deborah A DeMott 'Beyond Metaphor: An Analysis of Fiduciary Obligation' (1988) *Duke Law Journal* 879; Tamar Frankel, 'Fiduciary Duties as Default Rules' (1995) 74 *Oregon Law Review* 1209.

[77] See eg, Melvin Aron Eisenberg, 'The Structure of Corporation Law' (1989) 89 *Columbia Law Review* 1461, 1474-1481.

shareholders seek to opt-out from the duties, they cannot be given the power to consent on behalf of the company because of conflict of interest. Rather, consent should be provided by the company comprising both (1) a committee consisting of at least three non-executive independent directors and (2) disinterested shareholders.

As to who a disinterested shareholder is, it is suggested that a disinterested shareholder: (a) should not have any actual or potential conflict of interest and should there be such a conflict, to make a full and frank disclosure to the committee of independent directors who must assess the nature, scope and materiality of the conflict and then decide whether to allow the shareholder to vote despite the conflict of interest; and (b) should not be connected[78] to the controlling shareholder who is applying to opt-out.

In order to opt-out from the default position, the controlling shareholder must seek and obtain approval from both the committee of independent directors and disinterested shareholders; the opt-out will not be successful if one entity approves but the other rejects. Once the company has received the request from the controlling shareholder to opt-out from the default position, the company has to make a public announcement. Subsequently, a committee of independent directors has to be specially convened to decide whether to approve or reject the shareholder's request to opt out. This committee has to (a) set out in writing explaining with sufficient detail whether the opt out is in the best interests of the company, the scope of the opt-out (i.e. which are the fiduciary duties that will be opted out and whether they are opted out in all or only in certain prescribed circumstances), the duration of the opt-out (i.e.

[78] By "connected", it means (a) the shareholder who is giving the consent is a family member of the shareholder who is applying to opt-out; (b) the shareholder who is giving the consent is a trustee of any trust in which either the shareholder who is applying to opt-out, or the latter's family member, is a beneficiary; (c) the shareholder who is giving the consent is a director of another company of which the shareholder who is applying to opt-out is a controlling shareholder; or (d) the shareholder who is giving the consent is in a partnership with either the shareholder who is applying to opt-out or the latter's family member, with partnership defined under the respective jurisdiction's partnership legislation. The definition of connected here is adapted from the definition of connected in HK CO, s 486; MY CA, s 197; and SG CA, s 25D.

how long will the opt-out last), and whether they approve or reject the opt-out; and (b) advise the disinterested shareholders on how they should vote. Such a detailed and careful assessment will assist the disinterested shareholders in their deliberation and decision. As a result, any consent given by the disinterested shareholders will be informed. The detailed assessment provided by the special committee of independent directors will also address the problem of free rider and collective action problem as it will save the disinterested shareholders considerable time and expenses in gathering and analysing information (but this should not completely obviate the need for the disinterested shareholders to carry out their own independent assessment). Finally, a public announcement of the outcome of the application for opt-out has to be made as soon as practicable.

One concern is that the independent directors may be subject to pressure by the controlling shareholder to approve the opt-out. After all, the power to appoint, dismiss and re-appoint lies with the controlling shareholder. This concern can be addressed because the default position is that controlling shareholders are subject to the duty to act in good faith in the company's best interests. As long as consent has not been given to the controlling shareholder to opt out from the fiduciary duties, it remains subject to them. Thus, for example, if the independent directors decide not to give consent, the controlling shareholder could be in breach of the best interest duty if it subsequently dismisses them. Or should the controlling shareholder exert influence on the directors to give consent, it could be in breach of the duty to act in good faith in the company's best interests.

The other concern relates to whether the independent directors are indeed independent in the four jurisdictions. This issue has been examined in Chapter 3. As long as serious doubts concerning the independence of the independent directors remain, the use of independent directors as a mechanism to provide consent to the opt-out is called into question. Given that any consent given has to be independent and fully informed, the absence of independent consent undermines the claim that controlling shareholders should be given the right to opt-out.

Even if the concern regarding the independence of independent directors is addressed, there is the concern that the consent given by the independent directors and disinterested shareholders may not be fully informed. This is because it is one thing to give consent to opt-out of the fiduciary duties with respect to a specific circumstance or transaction, or for a specific period of time. It is another thing to give a blanket consent to opt-out of the fiduciary duties for all circumstances and transactions and with no time limitation whatsoever. The independent directors and the disinterested shareholders may not fully understand the significance and implication of giving such a blanket consent in relation to whether it is in the best interests of the company. It is suggested that there ought to be a sunset provision such that the opt-out will expire after, for example, one year, so that the controlling shareholder is required to renew the opt-out, and the independent directors and disinterested shareholders can make a fresh determination as to whether to give the consent.

In any event, if the legislature decides not to allow controlling shareholders to opt-out of fiduciary duties, or if the legislature allows opt-out, but the controller is not able to obtain consent from both the independent directors and disinterested shareholders, it will be subject to fiduciary duties.

2. Managing liabilities

The other strategy is for the legislature to impose a mandatory law that subjects controlling shareholders to fiduciary duties but provide for a basket of mechanisms to manage the liabilities that may arise from the breach of the duties, namely, ratification, insurance, indemnity, and application to court for relief. These mechanisms are similar to those used to manage directorial liabilities. They will each be analysed in turn.

Regarding ratification, a key issue is whether the votes of the wrongdoer (i.e. the controlling shareholder) should be included or excluded in the resolution passed by the general meeting. In Singapore[79], Malaysia[80] and India[81], the law does not require the votes of the wrongdoer, i.e. the director who has breached the duties, to be disregarded. By contrast, in Hong Kong[82] (and the UK[83]), the vote of the shareholder who is the delinquent director will be disregarded. In other words, only the votes of the disinterested shareholders will be counted. To ensure consistency with the law governing ratification of breaches of directors' duties, the respective jurisdiction may adopt the same approach with regards to ratification of breaches of shareholders' duties (unless there are reasons for adopting a different approach). That said, the three Asian jurisdictions should adopt the Hong Kong position under which the vote of the delinquent director is to be disregarded. This means that the vote of the delinquent shareholder should be disregarded too when it seeks to have its breach of duty ratified by the general meeting.

[79] Singapore has no statutory provision stipulating how ratification should be carried out. So the common law ratification which allows the shareholder who is the delinquent director to ratify his own acts will apply: *North-West Transportation Co Ltd v Beatty* (1887) 12 App Cas 589; *Raffles Town Club Pte Ltd v Lim Eng Hock Peter* [2013] 1 SLR 374 [42].

[80] Note that although the law does not require the wrongdoer's votes to be excluded, leading commentators have said that the ratification will be invalid if it is oppressive i.e. exercised by the wrongdoer itself. See Aiman Nariman Mohd Sulaiman and Effendy Othman, *Malaysia Company Law: Principles and Practices* (Wolters Kluwer 2015) [12.093], [13.033].

[81] India has no statutory provision stipulating how ratification should be carried out. So the common law ratification which allows the shareholder who is the delinquent director to ratify his own acts will apply: *Bakemans Industries Pvt Ltd v New Cawnpore Flour Mills* AIR 2008 SC 2699 [61].

[82] HK CO, s 473(3).

[83] UK Companies Act 2006, s 239(4).

Another issue with ratification is whether there are some acts which cannot be ratified under the law. The general meeting cannot ratify illegal acts, i.e. acts which are prohibited by the statute or common law. For example, the general meeting cannot ratify breaches of directors' duties where those breaches occurred in a situation in which the director is required to have regard for the creditors' interests.[84] Similarly, for example, if the controlling shareholder approved a major transaction involving a sale of the company's assets when the company was near insolvent, the controlling shareholder could be in breach of the duty to act in the best interests of the company (defined as the creditors' interests) and the general meeting should not be allowed to ratify this breach. The difficulty however is whether the general meeting can ratify acts which amount to a fraud on the minority,[85] or more accurately put, fraud on the company.[86] It has been said that the general meeting cannot ratify acts which amount to misappropriation of 'money, property or advantage which belong to the company or in which the other shareholders are entitled to participate.'[87] This implies that the pursuit of corporate opportunities (or at least certain types of corporate opportunities) by the controlling shareholder may constitute an unratifiable act.

It is suggested that to solve the problem of unratifiable breach pertaining to fraud on the minority, one should consider following the UK and Hong Kong statutory provisions under which the votes of the interested director in favour of the ratification are disregarded. Thus, the votes of the delinquent controlling shareholder should be disregarded. This is because it has

[84] *West Mercia Safetywear Ltd v Dodd* [1988] BCLC 250 (endorsing *Kinsela v Russell Kinsela Pty Ltd* (1986) 4 ACLC 215, 224); *Chintung Futures Ltd v Arthur Lai Cheuk Kwan* [1994] 1 HKLR 95; *Liquidators of Progen Engineering Pte Ltd v Progen Holdings Ltd* [2010] 4 SLR 1089 [48]; *Bakemans Industries Pvt Ltd v New Cawnpore Flour Mills* AIR 2008 SC 2699 [61].

[85] *Burland v Earle* [1902] AC 83, 93; *Atwool v Merrywweather* (1867) LR 5 Eq 464n; *Menier v Hooper's Telegraph Works* (1874) 9 Ch App 350; *Cook v Deeks* [1916] 1 AC 554.

[86] Len Sealy and Sarah Worthington, *Sealy and Worthington's Cases and Materials in Company Law* (10th edn, OUP 2013) 640.

[87] *Burland v Earle* [1902] AC 83, 93.

been said that under the UK and Hong Kong statutory provisions on ratification of directors' breach of duties, the general meeting can ratify any acts, including those that amount to fraud on the minority, except for those acts that are prohibited by the law or where creditors' interests are at stake.[88] Once the wrongdoer's vote is disregarded, the problem of fraud on the minority should no longer be relevant because the root of the problem lies with the wrongdoers voting to approve their own misappropriation of the company's property.[89]

Turning to insurance, to the extent that the laws in the four common law countries in Asia permit the company to effect insurance for directors in relation to breaches of duties to the company, the same treatment should be afforded to controlling shareholders. For example, under Hong Kong law, in relation to any breach of duty by directors against the company, the company can effect insurance for directors against (i) any liability to any person attaching to the director; or (ii) any liability incurred by the director in defending any proceedings taken against the director.[90] Under Singapore law, the company can effect an insurance for any director against any liability attaching to him in connection with any breach of duty in relation to the company.[91]

In relation to indemnity, the approach to be taken to controlling shareholders should not be different from that taken towards directors. For example, subject to certain exceptions,

[88] Brenda Hannigan, *Company Law* (4th edn, OUP 2016) 541-2; Simon Mortimore QC (ed), *Company Directors, Duties, Liabilities and Remedies* (OUP 2013) [20.32], [20.56] and [22.01]; Paul Davies and Sarah Worthington, *Gower and Davies' Principles of Modern Company Law* (9th edn, Sweet & Maxwell 2012) [16-99]; David Chivers QC and others (eds), *The Law of Majority Shareholder Power: Use and Abuse* (OUP 2008) [7.19]; Stefan HC Lo and Charles Z Qu, *Law of Companies in Hong Kong* (2nd edn, Sweet & Maxwell 2015) [8.181].

[89] But this solution may not be politically acceptable to the controlling shareholders if their votes are disregarded.

[90] HK CO, s 468(4).

[91] SG CA, s 172A.

the company can indemnify directors for their liabilities to third party.[92] The same treatment should be afforded to the controlling shareholders.

Finally, given that the court can relieve a director either wholly or partly from liability for breach of duties if the director has acted honestly and reasonably and ought fairly to be excused for the misconduct having regard to all the circumstances of the case[93], the same treatment should be afforded to the controlling shareholders.

B. Courts

The previous section analyses how the legislature could impose fiduciary duties. If fiduciary duties could not be imposed via the legislative route, this section examines how courts could do so. Courts cannot simply impose fiduciary duties on controlling shareholders without explaining how it coheres with existing case law and why it is a desirable development of the law. In other words, if a claimant wishes to persuade the court to impose fiduciary duties on controlling shareholders, what are the arguments that should be put forward.

Turning first to the issue of how courts could impose fiduciary duties, there are two main approaches. The first is that courts could impose fiduciary duties on controlling shareholders if the claimant can prove that they are shadow or de facto directors. The problems with using the route of shadow or de facto directors have been examined in Chapter 3 and I will not repeat them here. Rather, I will look at the second approach, namely, courts could impose fiduciary duties where the particular facts and circumstances warrant the imposition of

[92] HK CO, s 469; SG CA, s 172A; MY CA, ss 289(3) and 289(4); IN CA, s 91.

[93] HK CO, s 902-904; SG CA, s 391; MY CA, s 581; IN CA, s 463.

the duties.[94] There are three main types of factual matrices which justify the imposition of fiduciary duties by courts: (i) where a fiduciary relationship arises; (ii) where there is a legitimate expectation; and (iii) where there is an express or implied undertaking. Support for each of these factual matrices can be found in the case law and scholarly research.

1. Fiduciary relationship

As examined earlier, courts can impose fiduciary duties where a fiduciary relationship arises from the facts.[95] A fiduciary relationship arises when one party (the fiduciary) exercises discretionary power over another person (the beneficiary) and it affects the significant interests of the latter.[96] It has also been said that the elements of dependence, inequality and vulnerability are usually but not necessarily have to be all present.[97] For example, it has been said that dependence or vulnerability is merely an indicator and not a necessary condition for a fiduciary relationship to exist.[98] The relationship between the controlling shareholder and the company can be framed as a fiduciary one, which has been examined earlier. When controlling shareholders exercise their discretionary voting powers to: appoint and dismiss directors, dictate to or overrule the directors, exercise their management powers (if provided for in the

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[94] *Chirnside v Fay* [2006] NZSC 68 [75]. See also John McGhee, *Snell's Equity* (32nd edn, Sweet & Maxwell 2010) [7005]. The fact-based approach has to be contrasted with the status-based approach where courts impose fiduciary duties if the relationship falls within established categories of relationship (such as trustee-beneficiary, director-company and lawyer-client).

[95] See eg, *Guerin v Canada* [1984] 2 SCR 33 (SSC) 341; *Lac Minerals Ltd v International Corona Resources Ltd* [1989] 2 SCR 574 (SCC) 646; *Hospital Products Ltd v United States Surgical Corporation* [1984] 156 CLR 41 (HCA) 142; Miller, "The Fiduciary Relationship" (n 1).

[96] Miller, "A Theory of Fiduciary Liability" (n 1) 262; Miller, "The Fiduciary Relationship" (n 1) 69.

[97] Miller, "The Fiduciary Relationship" (n 1) 72-3; *Frame v Smith* [1987] 2 SCR 99, 136.

[98] *Hodgkinson v Simms* [1994] 3 SCR 377, 405; *Hospital Products Ltd v United States Surgical Corp* (1984) 156 CLR 41, 97.

constitution), authorise or ratify breaches of directors' duties, and approve major transactions, these voting decisions could materially and adversely affect the company's interests, and thus the company is vulnerable to the exercise of those voting powers by the controlling shareholder. Even if controlling shareholders do not exercise formal, i.e. voting power, but exercise informal power through the exertion of influence on the company, and as a result, the controlling extracted private benefits of control, the elements that give rise to a fiduciary relationship would also arise.

2. Legitimate expectation

The second factual matrix which could justify the imposition of fiduciary duties is when courts find that one party has a legitimate expectation that the other party will act in the former's interests.[99] It has been said that the '[fiduciary] concept encaptures a situation where one person is in a relationship with another which gives rise to a legitimate expectation, which equity will recognise, that the fiduciary will not utilise his or her position in such a way which is adverse to the interests of the principal.'[100] This has been endorsed by the Law Commission of England and Wales which states that '[t]he key test [for a fiduciary] is whether there is a

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[99] See eg, Paul Finn, 'The Fiduciary Principle' in Timothy G Youdan (ed), *Equity, Fiduciaries and Trusts* (Law Book Co 1989) 46: 'What must be shown … is that the actual circumstances of a relationship are such that one party is entitled to expect that the other will act in his interests in and for the purposes of the relationship. Ascendancy, influence, vulnerability, trust, confidence or dependence doubtless will be of importance in making this out, but they will be important only to the extent that they evidence a relationship suggesting that entitlement.'

[100] *Arklow Investments Ltd v Maclean* [2000] 1 WLR 594, 598.

legitimate expectation that one party will act in another's interest.'[101] But the Law Commission did not spell out when there is a legitimate expectation. It mentioned that 'discretion, power to act and vulnerability are indicators of such an expectation.'[102]

Given that they are indicators and are non-exclusive, courts should not be inhibited from developing the circumstances or factors that give rise to legitimate expectation. It is suggested that courts could recognise this circumstance as giving rise to a legitimate expectation: when the personal interests of the controlling shareholder conflict with those of the company (or where there is a real sensibility of conflict), and the controller exercises formal power (i.e. voting) or informal power (i.e. influence) over the company.

3. Consensual undertaking

Finally, fiduciary duties arise when one person expressly or impliedly undertakes to act on behalf of another on a matter.[103] It might be said that the controlling shareholder has not undertaken to act on behalf or in the interests of the company. However, although they have not made an express undertaking, the law will imply an undertaking if the person by his words, conduct or position give rise to a reasonable understanding or expectation that he would behave

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[101] UK Law Commission, *Fiduciary Duties of Investment Intermediaries* (Law Commission No 350) (1 July 2014) para 3.24.

[102] Ibid.

[103] *Bristol and West Building Society v Mothew* [1998] Ch 1, 18.

in a particular way.[104] It has been said that the more power that one person has over the other, and the more vulnerable one is to the other, the more likely that a reasonable person would have such an expectation.[105]

As the foregoing analysis demonstrates, in view of controlling shareholders' significant powers, the tunneling by controllers, the deficiencies in the current law regulating RPTs, and the conflicts of interest between them and the company that are not regulated by the law but which could give rise to extractions of private benefits of control, it is reasonable for the law to imply an undertaking.

Nevertheless, whichever fact-based approach the courts decide to adopt (i.e. whether fiduciary relationship, legitimate expectation or consensual undertaking), they have to directly address the proposition that votes are property rights and shareholders can vote as they please. This proposition has been debunked in Chapter 2.

C. Stock exchange

Should a stock exchange decide to impose fiduciary duties on controlling shareholders, it has to address the concern that it will face opposition from the controlling shareholders and that companies may be disincentivised to list on the exchange. These two concerns are similar to those in relation to the legislature imposing the fiduciary duties. To address these two concerns, the stock exchange can come up with two-tier listing standards: the first tier imposes

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[104] James Edelman, 'When Do Fiduciary Duties Arise?' (2010) 126 *Law Quarterly Review* 302, endorsed in, for eg, *F&C Alternative Investments (Holdings) Ltd v Barthelemy* [2012] Ch 613; *Vivendi SA Centenary Holdings III Ltd v Richards* [2013] EWHC 306 [137] (Ch).

[105] Edelman, ibid 317.

fiduciary duties and the second tier does not. Companies that are currently listed on the stock exchange can choose to remain in the second tier or can choose to migrate to the first tier. Companies that are considering whether to list can choose either the first or second tier.

Arguably the most famous and most successful example of such multi-tiered listing standards or what is known as dual regulatory regime is Brazil's Sao Paulo Stock Exchange which has four levels of listing, with the highest level being that of Novo Mercado.[106] The Sao Paulo Stock Exchange implemented this reform in order to attract more listings by enhancing minority shareholder protection while reducing or bypassing opposition from the controlling shareholders. The Sao Paulo Stock Exchange marketed Novo Mercado as having superior corporate governance. There are a number of differences in the listing requirements in each of the four levels. The most importance difference is that companies listed on the Novo Mercado are prohibited from having dual class shares, whereas companies listed on the other three levels are allowed to have them. The listing rules also restrict the ability of companies to exit Novo Mercado. The purpose is to ensure that companies listed on Novo Mercado are committed to a high degree of corporate governance. Further, the Stock Exchange is given the power to impose fines and suspend the trading of the shares of those companies that have flouted the listing requirements of Novo Mercado. One study found that 24.5% of companies are listed on the Novo Mercado, which account for 23.7% of the market capitalisation and 33.9% of the trading volume.[107]

In terms of the mechanics of the first-tier under which fiduciary duties are imposed, it is suggested that the stock exchange can require the controlling shareholder to enter into a written and legally binding agreement with the listed company which provides that the

[106] Ronald J Gilson and others, 'Regulatory Dualism as a Development Strategy: Corporate Reform in Brazil, the United States, and the European Union' (2011) 63 *Stanford Law Review* 475, 482-501; Marina Pargendler, 'State Ownership and Corporate Governance' (2012) 80 *Fordham Law Review* 2917, 2962-268.

[107] Ibid 498.

controlling shareholder has to comply with the fiduciary duties.[108] The agreement must also stipulate that the controlling shareholder and its associates shall not do anything which would hinder the company's compliance with the listing rules. Under this suggested listing rule, the company and all of the directors will be required to submit to the stock exchange, every quarterly, a statement signed and certified by each of them, stating that firstly, the company has entered into the agreement with the controlling shareholder, and secondly, the controlling shareholder has complied with the terms of the agreement. The listing rules could subject the company and/or the directors to civil sanctions for the failure to provide the certification or the provision of false certification. The sanctions can range from informal ones (such as private or public criticism) to formal ones (such as fines on the company and the directors, an order directing the company to take certain action, and suspension from trading). Failure to provide the certification or providing false certification will not only constitute a breach of the listing rules, but also a breach of directors' duties. Under this suggested listing rule, the burden is on the directors to monitor the behaviour of the controlling shareholders. Given that the controlling shareholders are subject to fiduciary duties when they exercise corporate powers, particularly the power of appointing and dismissing directors, as well as when they exert influence on the directors, the latter should not be afraid of monitoring the behaviour of the controllers.

[108] This proposal is adopted with modifications from the UK FCA LR 6.1.4B, D. But note that in the UK, sovereign controlled companies are exempted from the requirement (1) to have a "relationship agreement" between the state and the issuer and (2) to have disinterested shareholder approval of any RPTs between the state and the issuer. The relationship agreement essentially requires (i) transactions with the controlling shareholder to be conducted on arm's length and normal commercial terms, (ii) no action to be taken by the controlling shareholder (or its associates) to prevent the listed company from complying with its listing obligations, and (iii) neither the controlling shareholder nor its associates to propose a shareholder resolution which appears to be intended to circumvent the proper application of the listing rules. See Roger Barker and Iris H-Y Chiu, 'Protecting Minority Shareholders in Blockholder-Controlled Companies – Evaluating the UK's Enhanced Listing Regime in Comparison with Investor Protection Regimes in New York and Hong Kong' (2015) 10 *Capital Markets Law Journal* 98.

There are, however, three disadvantages to this dual regulatory listing regime. First, a jurisdiction that has such a regime is in effect sending a signal to investors that there is a lower level of investor protection in companies under the existing regime. This is likely to increase the cost of capital and reduce liquidity for those companies. Second, the entrenched and pervasive problem of extractions of private benefits of control will not be properly addressed. Finally, it could set an undesirable precedent for corporate legal reforms: going forward, controlling shareholders (particularly the government) may insist on preferential treatment and seek to be excluded from regulations that it finds disadvantageous but which will benefit the company, minority investors or society.

To conclude, in this chapter, I have analysed three key issues, i.e. when the fiduciary duties should be imposed, who should impose the fiduciary duties, and how the duties could be imposed. Regarding the first issue, my most important point is that fiduciary duties should be imposed when controlling shareholders exercise formal (i.e. corporate) power, and when they exercise informal (i.e. influence) power and but for their influence, the company would not have made the decision that benefitted them but which is at its expense. Regarding the second issue, I have evaluated the costs and benefits of having the legislature, courts and stock exchange impose the duties. While there is no definitive answer as to which institution should impose the duties given that each has its own pros and cons, my analysis leans towards the stock exchange. Regarding the final issue, I have examined how the legislature, courts and stock exchange could impose the duties. The legislature can do so by imposing either a default rule which allows for opt-out or a mandatory rule which contains a basket of mechanisms to ameliorate the consequences of liability. Courts can impose the duties using two approaches, the first of which is to characterise controllers as shadow or default directors, and the second is to impose the duties when the particular facts warrant doing so. Finally, stock exchange can impose the duties by having a two-tier listing regime, an existing one without the fiduciary duties and a new one with the duties.

DPHIL CHAPTER 6: ENFORCEMENT

I. Private enforcement
   A. Informal
   B. Formal
      1. Law suit by directors
      2. Derivative action
         a. Common law
         b. Statutory action
         c. Disincentives and reforms
      3. Oppression/Unfair prejudice
         a. Limitations with oppression/unfair prejudice
         b. Comparison with derivative action
II. Public enforcement
   A. Hong Kong
   B. India
   C. Singapore
   D. Malaysia
III. Conclusion

To begin, it is necessary but insufficient that we have effective 'laws on the books'. The law has to be backed up by credible enforcement ('law in action').[1] It has been demonstrated that there is a strong correlation between enforcement and financial market development.[2] Substantive law – law on the books – while important, does not account for the differences in the financial market development in different countries.[3] Further, the lack of effective enforcement will increase the cost of capital for companies as investors will demand a higher premium for their investments. Given the importance of enforcement, this chapter proceeds on the assumption that fiduciary duties should be or have been imposed on controlling

[1] Simeon Djankov and others, 'The Law and Economics of Self-Dealing' (2008) 88 *Journal of Financial Economics* 430; Rafael La Porta and others, 'What Works in Securities Laws?' (2006) 61 *Journal of Finance* 1; John C Coffee, Jr, 'Law and the Market: The Impact of Enforcement' (2007) 156 *University of Pennsylvania Law Review* 229; Howell E Jackson and Mark J Roe, 'Public and Private Enforcement of Securities Laws: Resource-Based Evidence' (2009) 93 *Journal of Financial Economics* 207.

[2] Coffee, Ibid.

[3] Ibid.

shareholders, and considers how breaches of those duties can be enforced using private and public mechanisms.

I first analyse informal private mechanisms. I then evaluate the costs and benefits of formal private mechanisms, comprising law suits by directors, derivative actions, and oppression/unfair prejudice actions. Regarding derivative actions, I argue that unless reforms to the existing regime are made, minority shareholders cannot effectively utilise this mechanism because of the lack of clarity and certainty in the law as well as the prohibition of contingency fees and class action suits. I then show that while there are problems with the oppression/unfair prejudice action, it should be easier and more likely for minority shareholders to pursue as compared to a derivative action. Nevertheless, private enforcement alone is insufficient. It has to be combined with public enforcement. Thus, I then examine whether breaches of fiduciary duties by controlling shareholders can be enforced using public mechanisms. I show that this is possible in Hong Kong and India, but in Singapore and Malaysia, the existing public mechanisms have to be reformed before this can occur.

I. Private enforcement

A. Informal

Where the wrongdoer is the controlling shareholder, the board could engage in a dialogue with the controller in order to come up with a mutually acceptable remedial measure. But given the formal and informal power wielded by the controller over the board, particularly in family-owned companies and state-owned enterprises in the four countries in Asia, there is a limit to what the directors can do.

An arguably more effective way is for the board to enlist the help of influential shareholders: these minority institutional shareholders may either hold a significant percentage of shares and/or be particularly influential in the investment community. If pressure by the board and the minority institutional shareholders on the delinquent controller to take remedial measures does not work, the institutional shareholders can threaten to sell their shares. But this approach has its limits too. If an institutional shareholder owns an insignificant and insubstantial amount of shares, say 1%, it is unlikely that the threat of selling shares or the actual exit will have a material and adverse impact on the company's share price, and hence the value of the shares held by the controller. Yet, the threat may become credible if the minority institutional shareholders act together and threaten to sell their shares. Another strategy is that the institutional shareholders can threaten to publicly criticise the controller. This may be more effective as public criticism by influential shareholders is likely to cause reputational harm to the controller. But such public criticism may cause a drop in the share price. This will also hurt the institutional shareholder's interests.

B. Formal

If private informal enforcement does not work, there are three formal private mechanisms, namely, law suits by directors, derivative actions by minority shareholders, and oppression (as is known in Singapore, Malaysia and India) or unfair prejudice (as it is known in Hong Kong).

1. Law suit by directors

Because fiduciary duties are owed by controlling shareholders to the company, the harm is done to the company, and thus, only the company is permitted to sue. Nevertheless, the board may not bring an action against the delinquent controller because the board may take the view that the costs of litigation exceed the benefits. The costs may include the financial cost of litigation, the potential negative publicity that it attracts, and the potential damage to the relationship between the company and the controlling shareholder, especially where the company and the controller has a business relationship. The benefits to the company include the financial gains in terms of the compensation that the court may award (which may not be substantial), and the deterrent effect of the litigation on the subsequent conduct of the controlling shareholder (which may not be significant).

2. Derivative action

a. Common law

If the board does not sue, an aggrieved minority shareholder can take action on the company's behalf, if it falls within the exceptions to the common rule of *Foss v Harbottle*[4], which is also known as the proper plaintiff rule. This rule and its exceptions have been endorsed in the common law countries in Asia.[5] Although Singapore, Malaysia and Hong Kong (but not

[4] (1843) 2 Hare 461, 67 ER 189.

India) have a statutory derivative action, only Malaysia has abrogated the common law derivative action. Thus, the common law action still applies to, and can be utilised in, Singapore and Hong Kong (but it is unlikely to be used at the same time as a statutory action). As India does not have a statutory action, the common law action continues to apply.

The first exception to *Foss v Harbottle* is that the wrongdoer has engaged in conduct that is *ultra vires* in the sense that it is unlawful for the company to do the act.[6] The law allows the minority shareholder to sue on the company's behalf to recover the money or property for the company. The second and more important, as well as commonly invoked, exception is fraud on the minority,[7] or more accurately put, fraud on the company as the wrong is done to the company under the proper plaintiff rule.[8] There is uncertainty as to what fraud on the company means. It depends on whether courts take a narrow view of fraud which refers to dishonesty, or a broad view which includes not only dishonesty but also equitable fraud[9] as well as breaches of directors' fiduciary duties[10] such as the no-conflict and no-profit rule.[11] Thus, applying this to the context of breaches of controlling shareholders' duties[12], if courts adopt a broad view of

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[5] See eg, *Waddington Ltd v Chan Chun Hoo* (2008) 11 HKCRAR 370 at 390; *Ting Sing Ning v Ting Chek Swee* [2008] 1 SLR(R) 197; *Abdul Rahim bin Aki v Krubong Industrial Park (Melaka) Sdn Bhd* [1995] 3 MLJ 417; *NVR Nagappa Chettiar v Madras Race Club* (1949) 19 Comp Cas 175.

[6] *Smith v Croft (No 2)* [1988] Ch 114, 177; *Burland v Earle* [1902] AC 83, 93.

[7] *Burland v Earle* [1902] AC 83, 93; *Edwards v Halliwell* [1950] 2 All ER 1064, 1067*; Waddington Ltd v Chan Chun Hoo* (2008) 11 HKCFAR 370, 380; *NVR Nagappa Chettiar v Madras Race Club* (1949) 19 Comp Cas 175; *Ting Sing Ning v Ting Chek Swee* [2008] 1 SLR(R) 197.

[8] KW Wedderburn, 'Shareholders' Rights and the Rule in Foss v Harbottle (continued)' (1958) 16 *Cambridge Law Journal* 93, 93-4.

[9] *Estmanco (Kilner House) Ltd v Greater London Council* [1982] 1 WLR 2, 12; *Vatcher v Paull* [1915] AC 372, 378.

[10] *Prudential Assurance Co Ltd v Newman Industries Ltd (No 2)* [1981] Ch 257, 316.

[11] *Atwool v Merryweather* (1867-68) LR 5 Eq 464; *Cook v Deeks* [1916] 1 AC 544.

[12] Note that because conduct by majority shareholders can amount to fraud on the company (*Menier v Hooper's Telegraph Works* (1873-74) LR 9 Ch App 350), it is possible for derivative action to be taken against controlling shareholders.

fraud, where a controller has failed to act in the company's best interests or has breached the no-conflict rule, it would have committed a fraud on the company.

Finally, under the first and second exception, where the disinterested shareholders (which will necessarily exclude the delinquent controller) have ratified the wrongdoing, the aggrieved minority shareholder cannot pursue the derivative action.[13]

b. Statutory action

Because the exceptions to the *Foss v Harbottle* can give rise to uncertainties, Hong Kong[14], Singapore[15] and Malaysia[16] (but not India which has no statutory but only a common law derivative action) have promulgated the statutory derivative action to simplify and clarify the law. There are several advantages to this statutory action. First, the claimant does not need to prove that it falls within the *Foss v Harbottle* exceptions. Second, unlike the UK statutory derivative action which requires the cause of action to relate to a breach of duty by a director[17], there is no such limitation in the provisions in Singapore[18] and Malaysia[19], and Hong Kong has expressly permitted the action to be brought for any misconduct committed against the company, not just by directors.[20] Thus, an action can be brought for a breach of fiduciary duties

[13] *Smith v Croft (No 2)* [1988] Ch 114, 185.

[14] Hong Kong Companies Ordinance (Cap 622) (HK CO), Part 14 Div 4.

[15] Singapore Companies Act (Cap 50) (SG CA), s 216A.

[16] Malaysia Companies Act 2016 (MY CA), s 347.

[17] UK Companies Act 2006, s 347. Note that while the cause of action has to be related to directorial breaches, the claimant can bring an action against a third party, either in addition to or in lieu of the delinquent director.

[18] SG CA, s 216A(2).

[19] MY CA, s 347.

by the controlling shareholder. Third, ratification by disinterested shareholders does not bar an action against the delinquent controller[21], unlike under the common law action. Fourth, the statutes make it clear that the court may order the company to pay reasonable legal fees, disbursements and costs to the complainant.[22] Although the court may also order the company to pay costs to the minority shareholder for bringing the action under the common law derivative action, the fact that this is now codified in the statute promotes certainty and clarity.

There is however a disadvantage with the statutory action (as compared to the common law action). The complainant bringing the action must apply for leave from the court to commence the action and the criteria that the court will use to decide whether to grant leave include whether there is a serious question to be tried (in the case of Hong Kong)[23], whether the complainant is acting in good faith (in the case of Singapore[24] and Malaysia[25]), and whether it appears *prima facie* in the company's interests for leave to be granted (in all three countries[26]). Under the common law action, the aggrieved shareholder can proceed to sue without asking the court for permission.

The problem with the good faith requirement (in Singapore and Malaysia) is that case law shows that it substantially overlaps with the requirement that the derivative action is *prima facie* in the company's interests. This is because the good faith requirement will not be satisfied if the court takes the view that the action is not pursued to advance corporate interest or purpose

[20] HK CO, ss 732(1), 731.

[21] HK CO, s 734(1); SG CA, s 216B; MY CA, s 349.

[22] HK CO, s 738; SG CA, s 216A(5)(c); MY CA, s 350(d) and (e).

[23] HK CO, s 733(1)(b)(i).

[24] SG CA, s 216A(3)(b).

[25] MYCA, s 348(4)(a).

[26] SG CA, s 216A(3)(c); MY CA, s 348(4)(b); HK CO, s 733(1)(a).

(the meaning and application of which is contestable).[27] It has also been said that in order for the court to conclude that the complainant has acted in good faith, the court has to be at least satisfied as to the propriety of the complainant's purpose, and whether granting the leave appears to be in the company's interests.[28]

As for the requirement concerning the company's interests, there is uncertainty regarding the standard for determining the company's interests. For example, in Singapore, there is case law that states that the complainant has to show that the action has objective legal merits, i.e. is not frivolous or vexatious[29], which is a low standard of proof. Yet, there is also case law that distinguishes legal merits and commercial merits, and subjects the complainant to the latter higher standard.[30] In Malaysia, it has been said that the test the court used is 'whether an intelligent and honest person in the position of the director could have reasonably believed that the decision was for the benefit of the company.'[31] This seems to be a high standard, and is similar to the Singapore case law that requires the complainant to prove that the action has commercial merits. In Hong Kong, while case law states that the court should not decide on the merits of the claims at the stage of leave[32], courts have not articulated a clear and workable test. Thus, although the statutory action has removed the uncertainty surrounding the *Foss v Harbottle* exceptions, it has given rise to other uncertainties.

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[27] *Ang Thiam Swee v Low Hian Chor* [2013] 2 SLR 340 [9], [13]; *Pang Yong Hock v PKS Contracts Services Pte Ltd* [2004 3 SLR(R) 1 [20]. Hans Tjio and others, *Corporate Law* (Academy Publishing 2015) [10.063].

[28] *Celcom (M) Bhd v Mohd Shuaib Ishak* [2011] 3 MLJ 636.

[29] *Ang Thiam Swee v Low Hian Chor* [2013] 2 SLR 340 [55-56].

[30] *Pang Yong Hock v PKS Contracts Services Pte Ltd* [2004] 3 SLR(R) 1 [21].

[31] Aiman Nariman Mohd Sulaiman and Effendy Othman, *Malaysia Company Law: Principles and Practices* (Wolters Kluwer 2015) [13.080]. The Malaysian provision stipulates "best interest of the company" instead of "interests of the company", the latter of which is reflected in the Singapore and Hong Kong provision.

[32] *Re Lucky Money Ltd* (unreported HCMP 05/2006, [2006] HKEC 1379) (CFI); Stefan HC Lo and Charles Z Qu, *Law of Companies in Hong Kong* (2nd edn, Sweet & Maxwell 2015) [10.056].

c. Disincentives and reforms

Apart from the uncertainties arising from the application of the rules on the common law and statutory derivative action, there are at least four disincentives related to the bringing of the common law and statutory derivative action. First, contingency fees are illegal in the four countries in Asia. Second, in India, there is a huge backlog of cases (with about 61,000 pending cases in the Supreme Court, and 94% of the cases in the High Court pending for 5 to 15 years) and on average, the courts take close to four years to dispose of the cases.[33] Third, any compensation or remedy that the court awards will go to the company, not to the affected shareholder itself. The shareholder will only benefit derivatively from any benefit that could be gained by the company from the law suit.

Fourth, the cost of the law suit (including the lawyer's fees and court fees) will be borne by the shareholder who initiated the derivative action, unless the court orders the company to pay costs to the shareholder who brought the action. The court is likely to do so if the shareholder has acted in good faith and has sought recovery on reasonable grounds.[34] But what is reasonable will depend on whether an independent board exercising the standard of care that is expected of a prudent business man would have taken the action.[35]

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[33] Arghya Sengupta, 'Hidden Factors That Slow Our Courts and Delay Justice' *The Economic Times* (29 March 2017); Vidhi Doshi, 'India's Long Wait for Justice: 27m Court Cases Trapped in Legal Logjam' *Guardian* (5 May 2016); Akanksha Jain, 'India Needs To Free Up Judicial Time, Address Delays To Make Doing Business Here Easy' *LiveLaw.In* (3 February 2018).

[34] HK CO, s 738(3). Although Singapore and Malaysian statutory provisions (unlike Hong Kong) do not have the requirements of good faith and reasonable grounds, those requirements are based on the decision of *Wallersteiner v Moir (No 2)* [1975] 1 All ER 849 and should also apply.

In view of the disincentives, the available published data shows that there are very few cases of derivative action. For example, in Hong Kong, from 2005 to 2016, a total of 36 derivative actions were brought, of which 24 (66%) were successful; this amounted to less than one action for every 225,000 companies incorporated in Hong Kong.[36] In India, from 1951 to 2011, only ten derivative actions were heard by the High Courts or the Supreme Court, of which only three were successful.[37] In Singapore, from 2000 to 2010, there appears to be about 15 derivative actions.[38] In Malaysia, from 2008 to 2015, there were 32 statutory derivative actions, of which only five succeeded.[39] The data on derivative action in listed companies is even more sparse: as of 2017, there appears to be four derivative actions in Hong Kong[40], and one in each of Malaysia[41], India[42] and Singapore[43].

To increase the incentives for minority shareholders to bring derivative action for breach of duties by controlling shareholders, two reforms should be made. The first is to clarify

[35] *Wallersteiner v Moir (No 2)* [1975] 1 All ER 849, 868-9.

[36] David Donald and Paul WH Cheuk, 'Hong Kong's Public Enforcement Model of Investor Protection' (2017) 4 *Asian Journal of Law and Society* 349, 369. Regarding statutory derivative action, it was found that there was not a single case in which the claimant succeeded in obtaining relief: Félix E Mezzanotte, 'The Unconvincing Rise of the Statutory Derivative Action in Hong Kong: Evidence From Its First 10 Years of Enforcement' (2017) 17 *Journal of Corporate Law Studies* 469.

[37] Vikramaditya Khanna and Umakanth Varottil, 'The Rarity of Derivative Actions in India: Reasons and Consequences' in Dan W Puchniak and others (eds), *The Derivative Action in Asia: A Comparative and Functional Approach* (CUP 2012) 80.

[38] Meng Seng Wee and Dan W Puchniak, 'Derivative Actions in Singapore: Mundanely Non-Asian, Intriguingly Non-American and At the Forefront of the Commonwealth"' in Dan W Puchniak, ibid, 355. The authors did not distinguish between common law and statutory derivative actions.

[39] Vivien Chen, 'The Statutory Derivative Action in Malaysia: Comparison with an Australian Judicial Approach' (2017) 12 *Asian Journal of Comparative Law* 281, 285.

[40] *Waddington Ltd v Chan Chun Hoo Thomas* [2013] HKEC 2013; *Yu Yuchuan v China Shanshui Investment Co Ltd* [2015] HKEC 437; *Hong Kong Zhongxing Group Company v Grand Field Group Holdings* [2014] HKCU 2729; *Veron International v RCG Holdings* [2015] HKCFI 1246 (unreported).

[41] *Dato' Low Tuck Choy v Datuk Lye Ek Seang* [2016] AMEJ 0671.

[42] *Northern Projects Limited v Blue Coast Hotels and Resorts Limited* 2007 Indlaw CLB 7.

[43] *Chua Swee Keng v E3 Holdings* [2015] SGHC 22. The key explanation for the lack of statutory derivative action in listed companies in Singapore is that prior to 2015, the statute only allowed Singapore private companies to pursue this action. This law has since been amended in 2015 to extend to listed companies.

the law in order to increase certainty and predictability, and the second is to introduce a statutory class action regime combined with contingency fee. And in the case of India, reforms have to be made to improve the efficiency and quality of the court system.

To increase the clarity and certainty of the law, the courts in Singapore and Hong Kong should first clarify the circumstances under which the common law and statutory derivative action could be and should be used.[44] Next, the courts in Singapore, Malaysia and Hong Kong should clarify the requirement of good faith (which applies only to Singapore and Malaysia) and company's interests (which applies to Singapore, Hong Kong and Malaysia) in relation to the application for leave for the statutory action. The courts in Singapore and Malaysia seem to have misconstrued the good faith requirement. The wording of the statute makes it clear that the requirement of good faith and the company's interest are separate and distinct. To give effect to the object of the statute (which is to facilitate and incentivise derivative actions given the difficulties of the common law derivative action, while deterring frivolous or vexatious law suits), it is suggested that good faith merely requires courts to be satisfied that the applicant subjectively (i.e. honestly) believes that it is bringing the action in order to remedy the wrongs done to the company, by verifying the complainant's subjective assertion against the available facts. It is neither necessary nor desirable for the courts to determine whether the action is in the company's interests in order to ascertain whether the complainant has acted in good faith. This is because doing so would be inconsistent with the wording of the statute as it in effect conflates the good faith requirement with that of the company's interests. Further, it would also indirectly subject the complainant to a more stringent requirement (i.e. the company's interests) without the benefit of the qualification (i.e. 'it appears'), the result of which is to make the

[44] It is unclear whether a common law action can be commenced if leave for statutory action has been rejected; nor is it clear whether leave for statutory action will be granted if the common law action has been struck out.

application for leave more burdensome for the complainant and hence disincentivise the complainant from suing.[45]

The requirement that the granting of the leave must *prima facie* be in the company's interests should be interpreted in light of two objectives: to give effect to the express wording of the statute, and to increase the incentive for the aggrieved shareholder to sue. The provision in Hong Kong merely requires the court to be satisfied that 'on the face of the application, it appears to be in the company's interests.'[46] The Singapore provision states: 'it appears to be *prima facie* in the interests of the company'[47] and the Malaysian provision 'it appears to be *prima facie* in the best interest of the company.'[48] The wording suggests that the standard is low: there should not be a trial within a trial. The court should not have to evaluate the merits of the claim. It is suggested that the test should be that once has the complainant has shown that the action is a legitimate one, i.e. it has 'a reasonable semblance of merit and is not one which is frivolous, vexatious or bound to be unsuccessful'[49], the complainant would have satisfied the statutory provision; the burden is then shifted to the defendant to show why the action would not be in the company's interests.[50]

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[45] It is more stringent because the separate requirement that the action has to be brought in the company's interests seems to require an objective evaluation by the courts, but the stringency is tempered by the qualification "it appears to be *prima facie*" in the company's interests. However, when the courts determine whether the applicant was acting in good faith by assessing whether the action is in the corporate interest, courts will not resort to the qualification.

[46] HK CO, s 733(1)(a).

[47] SG CA, s 216A(3)(c).

[48] MY CA, s 348(4)(b).

[49] *Urs Meisterhans v GIP Pte Ltd* [2011] 1 SLR 552 [25].

[50] *Fong Wai Lyn Carolyn v Antitrust (Singapore) Pte Ltd* [2011] 3 SLR 980; *Urs Meisterhans v GIP Pte Ltd* [2011] 1 SLR 552.

Regarding the statutory class action reform, Singapore, Hong Kong[51] and Malaysia could consider introducing a statutory class action regime for derivative action. Although none of the four Asian countries have a statutory class action regime for derivative suits, India has a statutory class action but only for oppression suits. Singapore, Hong Kong and Malaysia could consider adapting this class action mechanism for derivative actions. The Indian Companies Act 2013 provides that members of the company can bring an action before the National Company Law Tribunal (NCLT) (a quasi-judicial body that adjudicates issues on company law) 'if they are of the opinion that the management or conduct of the affairs of the company are being conducted in a manner prejudicial to the interests of the company or its members…'[52] Given that the NCLT is a specialised tribunal that deals with company law matters, it should be more efficient than the court system.

The members of the company can apply to the NCLT for an order[53] including but not limited to: restraining the company from breaching the constitution, statute or any applicable law; claiming damages or compensation or demanding any other suitable action from or against the company, its directors or any other person; and seeking any other remedy as the NCLT may deem fit. Although there is no express language in the statutory provision permitting the aggrieved shareholder to claim damages or compensation from the controller for breach of fiduciary duties, the broadly worded and 'catch-all-provision' in s 245(1)(h) – 'to seek any other remedy as the [NCLT] may deem fit' may be utilised by the aggrieved shareholder.[54]

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[51] The Law Commission in Hong Kong has proposed introducing a statutory class action regime by applying it for a start to consumer cases. See Law Reform Commission of Hong Kong Report, Class Actions (May 2012) [3.34].

[52] India Companies Act 2013 (IN CA), s 245(1).

[53] Ibid.

[54] Cf Vikramaditya Khanna, 'Enforcement of Corporate and Securities Laws in India: The Arrival of the Class Action?' in Robin Hui Huang and Nicholas Calcina Howson (eds), *Enforcement of Corporate and Securities Law: China and the World* (CUP 2017) 354.

Importantly, the Companies Act provides that failure to comply with the NCLT's order is a criminal offence under which the company may be fined and the officer of the company may be imprisoned (for up to three years) and fined.[55] Moreover, the provision requires all similar applications to be consolidated into a single application and the class members should be allowed to choose the lead applicant, but if no consensus is achieved, the NCLT shall appoint the lead applicant who will be in charge of the proceedings.[56] Finally, two class action applications for the same cause of action is prohibited.[57]

But there are restrictions on the use of this statutory class action regime that may make it difficult for the aggrieved shareholder to utilise it. One restriction is that there must be at least 100 members or such number as may be required by NCLT before the class action suit can commence.[58] Further, in considering the application, the NCLT has to consider a number of factors including whether the shareholders are acting in good faith or have any personal interest; and whether the act or omission involved has been authorised or ratified by the shareholders.[59] Moreover, the NCLT can impose costs on the applicant and reject the application if it finds that the application is frivolous or vexatious.[60]

The statutory restrictions are fair and sensible except for the requirement that there must be at least 100 members which may impose considerable cost for an aggrieved shareholder in a listed company to coordinate with the other affected shareholders. It is suggested that the fact

[55] IN CA, s 245(7).

[56] IN CA, s 245(5)(b).

[57] IN CA, s 245(5)(c).

[58] IN CA, s 245(3)(i)(a).

[59] IN CA, ss 245(4)(a), 245(4)(e).

[60] IN CA, s 245(8).

that the NCLT can impose costs on the applicant and reject the application if it is frivolous or vexatious is sufficient to ensure that that there is no abuse of the class action regime.

3. Oppression/Unfair prejudice

Because the duties owed by controlling shareholders are to the company and thus a breach of the duties is a corporate wrong, the aggrieved minority shareholder should not be permitted to use the mechanism of oppression (as is known in Singapore, Malaysia and India) or unfair prejudice (as is known in Hong Kong), which is a personal action, in order to address wrongs done to the company, as this would circumvent the rule in *Foss v Harbottle,* and hence amount to an abuse of process.[61]

However, there is an overlap between corporate action (i.e. derivative action) and personal action (i.e. oppression/unfair prejudice) as the interests of a shareholder (or some shareholders) could be harmed by corporate wrongs such as breaches of fiduciary duties. This overlap is evidenced in the numerous decisions in which breaches of directors' fiduciary duties gave rise to oppression/unfair prejudice actions.[62] Moreover, the overlap can also be seen in the orders that the court can make for giving relief in an oppression/unfair prejudice action: it can authorise the aggrieved shareholder to commence a derivative action or it can order

[61] *Re Chime Corp Ltd* [2004] 3 HKLRD 922; *Ng Kek Wee v Sim City Technology Ltd* [2014] 4 SLR 723 [63]-[64].

[62] See eg, UK cases: *Lloyd v Casey* [2002] 1 BCLC 454; *Fowler v Gruber* [2010] 1 BCLC 563; *Allmark v Burnham* [2006] 2 BCLC 437; *Re Baumler (UK) Ltd, Gerrard v Koby* [2005] 1 BCLC 92. Regarding the cases in the common law countries in Asia, see eg *Lim Swee Khiang v Borden Co (Pte) Ltd* [2006] 4 SLR(R) 745; *Low Peng Boon v Low Jaime* [1999] 1 SLR(R) 337; *Re Gee Hoe Chan Trading Co Pte Ltd* [1991] 2 SLR(R) 114; *Re Bondwood Ltd Development Ltd* [1990] HKLR 200; *Re Playmates Investments Ltd* [1996] 4 HKC 577; *Re Tai Lap Investment Co Ltd* [1999] 1 HKLRD 384; *Air Cool Window Tinting Film (M) Sdn Bhd v Lim Chien Wah & Air Cool Auto Marketing* (Civil Suit NoD-22NCC-1249-2010).

damages or restitution to be made to the company.[63] It would thus be appropriate for an aggrieved shareholder to bring an oppression/unfair prejudice petition in connection with wrongs done to the company (such as breach of fiduciary duties by controlling shareholders), if the whole gist of the complaint is not about the unlawfulness of the acts or omissions, such that the remedy provided to address corporate wrong is inadequate.[64]

Broadly speaking, any member of the company can invoke the oppression/unfair prejudice remedy if she can show that the company's affairs are being conducted in a manner unfairly prejudicial or oppressive to her interests. Despite the differences in the precise wording in the statutory provisions in each of the four common law jurisdictions in Asia, the underlying concern is with the conduct of the company which is unjustly detrimental to any member; there has to be 'visible departure from the standards of fair dealing.'[65] What constitutes unfairness is fact- and context-specific.

Although courts in the four common law countries in Asia have not articulated clear criteria as to what amounts to oppression or unfair prejudice, courts have relied on two indicia of oppression/unfair prejudice.[66] The first indicium consists of legal rights and obligations. For example, breaches of companies statute[67], company's constitution[68], listing rules[69], and

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[63] *Re Chime Corp Ltd* [2004] 3 HKLRD 922.

[64] *Re Charnley Davies Ltd (No 2)* [1990] BCLC 760.

[65] *Re Khong Thai Sawmill (Miri) Sdn Bhd* [1978] 2 MLJ 227, 229; *Owen Sim Liang Khui v Piasau Jaya Sdn Bhd* [1996] 1 MLJ 113; *Over & Over Ltd v Bonvests Holdings Ltd* [2010] 2 SLR 776 [77].

[66] *O'Neill v Phillips* [1999] 1 WLR 1092, 1098-1099.

[67] *Re a Co (No.005134 of 1986), ex p Harries* [1989] BCLC 383 (breach of the requirement of member approval for non-pro rata allotments of shares); *Re Bondwood Development Ltd* [1990] 1 HKLR 200 (numerous breaches of the requirement to keep proper accounts); *Re a Co (No.00789 of 1987) ex p Shooter* [1990] BCLC 384 (failure to hold general meetings and to let members approve accounts).

[68] *O'Neill v Phillips* [1999] 1 WLR 1092; *Re Mediavision Ltd* [1993] 2 HKC 629; *Re A and BC Chewing Gum Ltd* [1975] 1 WLR 579; *Re Harmer Ltd* [1959] 1 WLR 62; *Re Bondwood Development Ltd* [1990] 1 HKLR 200.

[69] *Luck Continent Ltd v Cheng Chee Tock Theodore* [2013] 4 HKLRD 181.

directors' fiduciary duties[70] have given rise to an oppression/unfair prejudice. Shareholders are entitled to expect that the powers conferred on directors will be exercised in accordance with the company's constitution, companies statute, and any applicable law. Thus, if the law on controlling shareholders' fiduciary duties is enshrined in the companies statute or listing rules, or if it is imposed by courts, a breach of that law may amount to oppression/unfair prejudice.[71]

The second indicium is equitable considerations which arise from an unwritten or informal understanding between the member and the company, which makes it inequitable to insist on legal rights.[72] Such equitable considerations usually involve 'a personal relationship or personal dealings of some kind.'[73] Such personal relationship usually arises in small companies – called quasi-partnerships – where there is a relationship of mutual trust and confidence among the members.[74] Absent such a relationship, shareholders in a listed company cannot reasonably expect anything more than the fact that directors will comply with their duties and the company's affairs will be conducted in accordance with the applicable laws and the company's constitution.[75] It has been held that the second indicium should not apply to the context of a listed company. This is because '[i]f the market in a company's shares is to have any credibility, members of the public company dealing in that market must it seems to me be entitled to proceed on the footing that the constitution of the company is as it appears in the

[70] (n 62).

[71] However, not all breaches, particularly if they are trivial, will result in prejudice and thus unfair prejudice*: Re a Co (No.00789 of 1987) ex p Shooter* [1990] BCLC 384, 393.

[72] *O'Neill v Phillips* [1999] 1 WLR 1092; *Ebrahimi v Westbourne Galleries Ltd* [1973] AC 360, 379.

[73] *Re Astec (BSR) plc* [1999] BCLC 556 at 588; *O'Neill v Phillips* [1999] 1 WLR 1092, 1101.

[74] *Ebrahimi v Westbourne Galleries Ltd* [1973] AC 360, 371.

[75] *Re Astec (BSR) plc* [1999] BCC 59.

company's public documents, unaffected by any extraneous equitable considerations and constraints.'[76]

a. Limitations with oppression/unfair prejudice

Apart from the limitation that not all breaches of fiduciary duties will necessarily result in oppression/unfair prejudice, there are at least four other limitations that may inhibit the success of this action.

First, there is uncertainty as to whether an isolated act will amount to oppression/unfair prejudice. For example, Indian courts have held that the acts must be continuous, up to the point of petition.[77] In Hong Kong, the previous companies statute specifically stated that the remedy is available whether the unfairly prejudicial conduct consists of an isolated act or a series of acts.[78] But this wording is absent in the current legislation.

Second, an aggrieved shareholder's disagreement with the decisions taken at the general meeting does not provide a basis for the oppression/unfair prejudice remedy.[79] The principle of majority rule applies, and thus, unless a minority shareholder can show that the controller has breached its fiduciary duties, commercial misjudgement or unwise decisions made by the controller will not give rise to oppression.

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[76] Ibid 67.

[77] *Shanti Prasad Jain v Kalinga Tubes Ltd* (1965) 35 Com Cases 351, 366-7.

[78] Hong Kong Companies Ordinance (Cap 32) (repealed), s 168A(2).

[79] *Re Tai Lap Investment Co Ltd* [1999] 1 HKLRD 384, 397; *Re Tri-Circle Investment Pte Ltd* [1993] 2 SLR 523, 534; *Balakrishnan Vairavapillai v Pantai Holdings Bhd* (2005) MSCLC 92, 936; *Central Government v Kopran Ltd* (2005) 125 Com Cases 495; (2004) 56 SCL 428 (CLB).

Third, the law draws a distinction between the company's conduct, on the one hand, and the conduct of shareholders or directors in their private capacities, on the other hand.[80] The oppression/unfair prejudice remedy does not cover the latter situation. Thus, purely intra-shareholder disputes that do not involve acts/conduct of the company will not be covered by oppression/unfair prejudice remedy.[81]

Fourth, in India, as a preliminary matter, the petitioner who brings the oppression action is required to show that the facts would justify winding up the company on the just and equitable ground. However, because doing so would unfairly prejudice the petitioner, the court will not award the remedy.[82] Moreover, the oppression remedy can only be pursued by a member who owns not less than 10% of the issued shares; or the action can only be pursued by at least 100 members or 10% of the total members.[83] These procedural restrictions make it very difficult for the oppression action to be pursued in India.

b. Comparison with derivative action

Nevertheless, despite these limitations, where there is an alleged breach of fiduciary duties by the controlling shareholder, it should be easier and more likely for the aggrieved shareholder to pursue an oppression/unfair prejudice action as compared to a derivative action

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[80] *Re a Co (No. 001761 of 1986)* [1987] BCLC 141, 148; *Re Unisoft Group Ltd* [1994] 1 BCLC 609, 622; *Re Ka Ka Realty Ltd* [2004] 1 HKLRD 832; *Lim Cheng Huat Raymond v Teoh Siang Teik* [1996] 3 SLR(R) 371 [58].

[81] For example, failure by a controlling shareholder to adhere to a pre-emption or transfer provision in the company's constitution does not amount to conduct of the company's affairs (*Re Coroin Ltd (No 2), McKillen v Misland (Cyprus) Investments* [2013] EWCA Civ 781), unless the failure is to exclude a minority from the company (*Graham v Every* [2015] 1 BCLC 41).

[82] IN CA, s 242(1)(b).

[83] IN CA, s 244(1)(a).

for two reasons. First, although the aggrieved shareholder has to pay the cost of litigation, the compensation (if awarded by the court) will go to her, and not to the company, unlike in a derivative action. Second, the remedies that the court can award for oppression/unfair prejudice are wide and flexible. The court may make any order that it deems fit for giving relief including but not limited to: regulating the conduct of the company's affairs in the future; directing or prohibiting any act or cancelling or varying any transaction or resolution; authorising civil proceedings to be brought in the name of or on behalf of the company; providing for the purchase of the shares of the petitioner by the company or other members; and winding up the company.[84] These are mere examples and the court can consider other remedies including but not limited to ordering the company or any other person to pay damages to the aggrieved member.[85] The court is not limited to reversing or rectifying the immediate wrongdoing, but can take action to prevent the conduct from occurring in the future.[86] In making the order, the court is permitted not only to take into account the interests of shareholders, but also those of others including but not limited to creditors.[87]

However, it may be said that because the most common remedy awarded by the court is the buy-out order, it is unlikely that an aggrieved shareholder of a listed company is in need of that remedy as she could sell her shares on the market. Thus, it may be said that the cost of bringing the action will exceed the benefit (i.e. the buy-out order). This may be one reason why there are very few oppression/unfair prejudice cases involving listed companies. To date, there

[84] SG CA, s 216(2); MY CA, s 346(2); HK CO, s 725(2); IN CA, s 245(1).

[85] HK CO, s 725(2)(b); IN CA, s 245(1)(g).

[86] *Re Bird Precision Bellows Ltd* [1985] BCLC 493, 499-500; *Grace v Biagioli* [2006] 2 BCLC 70.

[87] *Re Neath Rugby Ltd (No 2), Hawkes v Cuddy (No 2)* [2009] 2 BCL 427 [84]; *Fulham Football Club (1987) Ltd v Richards* [2012] 1 BCLC 335 [46].

appears to be four such cases in Hong Kong[88], three in Singapore[89], one in Malaysia[90], and two in India.[91]

Nevertheless, there are two situations where an oppression/unfair prejudice action is still valuable for a minority shareholder in a listed company. First, a long-term shareholder may wish to continue to remain in the company instead of having his shares bought out. What the shareholder wants is for the court to prohibit a particular act or to cancel or vary a particular transaction or resolution. Or it may want the court to order the controlling shareholder to do or refrain from doing something. Second, selling the shares on the market will not sufficiently protect the minority shareholder as the share price may have fallen significantly because the wrongdoing by the controller has been reported in the news. Thus, buy-out orders still have an important role to play.

The preceding analysis on private enforcement assumes that litigants will resort to the courts (or tribunals) to enforce their claims. It is suggested that in countries where the court system is very inefficient (such as in India), reforms should be made to the listing rules to give shareholders the ability to enforce their claims in arbitration, given that arbitral proceedings are generally known to be far more efficient.[92] For example, because of the ineffective

[88] *Luck Continent Ltd v Cheng Chee Tock Theodore* [2013] 4 HKLRD 181; *Yu Yuchuan v China Shanshui Investment Co Ltd* [2015] HKEC 437; *Passport Special Opportunities v Esun Holdings* [2011] 4 HKC 62; *Able Success Asia v China Packaging Group Company Limited* [2014] HKCU 1316.

[89] *Over & Over Ltd v Bonvests Holdings Ltd* [2010] 2 SLR 776; *Ezion Holding Ltd v Teras Cargo Transport Pte Ltd* [2016] SGHC 175; *The Wellness Group v OSIM* [2016] SGHC 64.

[90] *Kang Choon Leu @ Kang Chee Sim v Wintoni Group Berhad* [2016] AMEJ 1264.

[91] *Morgan Ventures Ltd v Blue Coast Hotels and Resorts Ltd* [2010] 155 Comp Cas 431; *Union of India (UOI) v Satyam Computer Services Ltd* [2009] 148 Comp Cas 252.

[92] See eg, Roger S Haydock, 'Civil Justice and Dispute Resolution in the Twenty-First Century: Mediation and Arbitration Now and for the Future' (2000) 27 *William Mitchell Law Review* 745; Keith N Hylton, 'Agreements to Waive or to Arbitrate Legal Claims: An Economic Analysis' (2000) 8 *Supreme Court Economic Review* 209; Steven Shavell, 'Alternative Dispute Resolution: An Economic Analysis' (1995) 24 *Journal of Legal Studies* 1.

commercial courts in Brazil, companies listed on the Novo Mercado in Brazil are subject to mandatory arbitration.[93]

However, private enforcement in itself is not adequate if the rules are unclear, the incentives for bringing claims are weak, the court system is not well-functioning, and public interest considerations are implicated. Effective enforcement also requires public enforcement to which we now turn.

II. Public enforcement

A. Hong Kong

There is no public enforcement mechanism that allows a regulator to enforce breaches of controlling shareholders' fiduciary duties *per se*. But there is an existing mechanism that allows the regulator to take action to address harms done to the company or to shareholders. It can be used to enforce breaches of controlling shareholders' fiduciary duties. Section 214 of the Securities Futures Ordinance authorises the Securities Futures Commission (SFC) to apply to the court for an order if the SFC finds that the company's business or affairs have been conducted in a manner (a) oppressive to any part of its members; (b) involving misappropriation of funds, fraud, misfeasance or other misconduct towards it or any of its members; (c) resulting in any of its members not having been given all the information with respect to its business or affairs that the member might reasonably expect; or (d) unfairly

[93] Ronald J Gilson and others, 'Regulatory Dualism as a Development Strategy: Corporate Reform in Brazil, the United States, and the European Union' (2011) 63 *Stanford Law Review* 475, 492-494.

prejudicial to any of its members.[94] The relief that the court can grant includes (a) requiring an act to be carried out or not to be carried out; (b) ordering the company to sue any person; (c) removing any director or officer of the company, or ordering any person not to directly or indirectly be concerned or participate in the company's management; and (d) making any order that the court considers appropriate such as regulating the company's business or affairs or ordering any member's shares to be bought out.[95]

Thus, where there is a breach of fiduciary duties by the controlling shareholder, this will amount to a misconduct towards the company under s 214(1)(b), and because there will usually be harms done to minority shareholders when the controller breaches its duties, it will amount to oppression or unfair prejudice under s 214(1)(a) and (d). The court has an array of remedies that it can deliver including but not limited to ordering the delinquent controller to take or cease taking certain action; ordering the company to sue the controller; ordering the controller not to be involved in the company's management; and ordering the minority shareholder's shares to be bought out.[96]

One study, however, finds that while s 214 has been available to the SFC for over 20 years, it has only used it 14 times.[97] Further, in the majority of cases in which the SFC used it (and mainly for the purpose of disqualifying delinquent directors), the companies had already been suspended from trading, were insolvent, or were facing other law suits.[98] There is no study explaining why the SFC has not used this mechanism more frequently or prior to the company's

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[94] Securities and Futures Ordinance (Cap 571), s 214(1).

[95] Ibid, s 214(2).

[96] Ibid.

[97] David C Donald and others, *A Financial Center for Two Empires: Hong Kong's Corporate, Securities and Tax Law in its Transition from Britain to China* (CUP 2014) 128.

[98] Ibid 128-129.

insolvency. There are several possible reasons. One obvious one is that in light of finite resources, the SFC has to make a judgment as to which violations warrant investigation and prosecution. After all, market manipulation, insider trading, prospectus misstatements, and regulation of financial intermediaries all fall within the scope of its supervision. The other reason which follows from the first is that it is arguably more efficient for the SFC to intervene at a later stage after the wrongdoing of the company and its agents have been proven in connection with other proceedings, such as after the company has been delisted by the stock exchange. In other words, the SFC may not need to incur the costs of investigation as this has already been borne by other regulatory authorities and the SFC can leverage on the findings made by other regulators (such as the stock exchange).

That said, the SFC has recently become more proactive in using s 214 by commencing legal proceedings against delinquent directors even when the company is not insolvent.[99] In those cases, the SFC not only successfully disqualified the delinquent directors, but also successfully sued them for disgorgement of profits and compensation.[100] If this trend continues, it is possible that SFC may also use s 214 to enforce breaches of fiduciary duties by controlling shareholders.

B. India

There is no public mechanism to enforce breaches of controlling shareholders' fiduciary duties per se. But there are two mechanisms that may be utilised to enforce such breaches. The

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[99] David C Donald and Paul WH Cheuk, 'Hong Kong's Public Enforcement Model of Investor Protection' (2017) 4 *Asian Journal of Law and Society* 348, 372-373.

[100] 'SFC Seeks Court Orders Against Chairman, Current and Former Directors of Minth Group Limited' *SFC News Release* (15 April 2014); 'SFC Obtains Court Orders for GOME to Receive $420 Million Compensation from Founder and Wife Over Breaches in Share Repurchase' *SFC News Release* (7 May 2014).

first is s 241(2) of the Companies Act which provides that if the government is of the view that the company's affairs are being conducted in a manner that is prejudicial to public interest, the government can apply to the National Company Law Tribunal (NCLT) for remedies.[101] Case law has not provided any clear definition or guidelines as to what 'public interest' means. It has been said that this term varies with time, the state of society and its needs.[102] It refers to the general welfare of the community, whose interests extend beyond those of shareholders to include other constituencies such as employees, consumers and the public in general.[103] This public enforcement mechanism has been used at least three times in high profile cases which involved breaches of directors' duties, misappropriation of funds, falsification of financial information and other types of fraudulent action.[104]

While it is possible for the government to use s 241(2) to enforce breaches of controlling shareholders' fiduciary duties, it will only do so if the public interest has been prejudiced. Judging by past enforcement actions, the breach has to be very serious and has to have a material and adverse impact not only on minority shareholders, but also other stakeholders. Thus, it is unlikely for the government to enforce breaches of controlling shareholders' fiduciary duties by invoking s 214(2) frequently.

If the government were successful in its enforcement action for breach of controlling shareholders' fiduciary duties, the remedies that the NCLT can award include but are not limited to: (a) the regulation of the company's affairs; (b) share buy-out; (c) the termination, setting aside or modification of any agreement between the company and any person; (d) the

[101] IN CA, s 241(2).

[102] Arvind P Datar and S Balasubramanian, *A Ramaiya Guide to the Companies Act* (18th edn, Lexis Nexis 2014) 4020.

[103] *Bhalchandra Dharmajee v Alcock Ashdown and Co Ltd* 1972 (42) CC 190.

[104] Jayshree P Upadhyay, 'Govt Moves to Take Over Unitech as NCLT Dismisses Company Board' *LiveMint* (9 Dec 2017).

imposition of costs as may be deemed fit by NCLT; (e) any other matter for which, in NCLT's opinion, it is just and equitable that provision should be made.[105] These wide-ranging remedies will allow the NCLT to address wrongs done to the company (remedy (a), (c) and (d)) and the aggrieved shareholder (remedy (b) and (d)). Importantly, the NCLT can impose costs on the delinquent controller.[106]

The second formal enforcement mechanism is that the complainant can initiate action before the Securities and Exchange Board of India (SEBI). The SEBI's central function is to protect investors' interests and to regulate the securities market.[107] Its jurisdiction covers not only securities regulation but also matters related to corporate governance; the scope of its power is wide which includes ensuring that there is no violation of laws that will impact on the interests of investors.[108] Thus, it is possible for the SEBI to take enforcement action for breaches of controlling shareholders' fiduciary duties. But the remedies that the SEBI will deliver are intended to address harms done to the investors, rather than harms done to the company (although there is nothing in the SEBI Act that will preclude the SEBI from doing so). The orders that the SEBI can impose, which could apply to an enforcement of breaches of controlling shareholders' fiduciary duties, include but are not limited to: (a) suspending the trading of the company's shares; (b) restraining any person from accessing the securities market and prohibiting any person from buying, selling or dealing in securities; and (c) impounding and retaining the proceeds or securities in respect of any transaction which is under investigation.[109] Further, the phrase 'any person… associated with the securities market' under

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[105] IN CA, s 242(2).

[106] IN CA, s 242(2)(l).

[107] Securities and Exchange Board of India Act, 1992 (as amended by the Securities Laws (Amendment) Act, 2014), s 11(1).

[108] Vikramaditya Khanna and Umakanth Varottil (n 37) 388.

[109] Securities and Exchange Board of India Act 1992, s 11(4).

s 11B(i) may be broadly construed to refer to shareholders such that the SEBI is empowered to issue such directions 'as may be appropriate in the interests of investors in securities and the securities market.'[110] Section 11B makes it clear that the SEBI's direction includes the power to disgorge the wrongful gain made or loss averted. Thus, under ss 11(4) and 11B, the SEBI may be allowed to disgorge the gains made by the delinquent controller who has breached its duties, to bar the controller from accessing the capital market, bar the controller from buying or selling any shares, and in the worst case, suspend the trading of the company's shares. Importantly, given that the SEBI has had a reputation for efficient enforcement[111], public enforcement is more advantageous than private enforcement.

C. Singapore

In Singapore, there is no public enforcement mechanism that can be used to enforce breaches of controlling shareholders' fiduciary duties. There is nothing comparable or similar to s 214 of the Hong Kong Securities Futures Ordinance or s 241(2) of the Indian Companies Act. Nor does the Monetary Authority of Singapore, which is responsible for the enforcement of securities laws, have the broad scope of powers that the SEBI has. The question of which public enforcement authority can enforce breaches of controlling shareholders' fiduciary duties depends in part on which authority – stock exchange or legislature – imposes duties on controllers. Nothing in the stock exchange rules permits actions to be taken against the

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[110] Ibid, s 11B(i)(a).

[111] G Sabarinathan, 'Securities and Exchange Board of India and the Regulation of the Indian Securities Market', IIM Bangalore Research Paper No. 309 (2012); Ajit Dayanandan and others, 'Effectiveness of SEBI's Complaints Redress Systems (SCORES) in India' (2015); Cf Dev Chatterjee, 'GIFT to Create Regulatory Crisis for RBI, SEBI: Mistry' *Business Standard* (23 February 2016).

controlling shareholder for breaches of duties. But currently, informal and formal enforcement tools are available to the stock exchange, which allows the exchange to take action against the company (such as issuing a private warning, fining the company, suspending trading and even delisting the company) and any Relevant Person by requiring the latter to rectify the consequences of contraventions. 'Relevant Person' is defined as 'an issuer, its directors, executive officers, and issue managers.'[112] It is suggested that the definition of 'Relevant Person' can be amended to include controlling shareholders.

If it is the legislature that imposes the fiduciary duties on controlling shareholders, it is likely to do so by amending the Companies Act. The regulatory authority in charge of administering the Companies Act is the Accounting and Corporate Regulatory Authority (ACRA).[113] However, ACRA has no blanket authority to enforce breaches of directors' duties in general (except when there is a failure to hold AGMs, failure to lay accounts at the AGM, failure to file annual returns, failure to provide information concerning the particulars of the directors and officer, or the provision of false information).[114] Thus, the relevant legislation has to be amended to specifically authorise ACRA to enforce breaches of controlling shareholders' fiduciary duties.

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[112] SGX LR 1401.

[113] Accounting and Corporate Regulatory Act (Cap 2A), s 6(1)(a).

[114] ACRA Enforcement Policy, para 16 <https://www.acra.gov.sg/Enforcement_Policy_Statement/> assessed 1 December 2018.

Malaysia has no public enforcement mechanism that is comparable or similar to that in Hong Kong or India, nor is there any existing public mechanism that can be utilised to enforce breaches of controlling shareholders' fiduciary duties. The situation in Malaysia is similar to that in Singapore in that first, the listing rules[115] have to be amended to permit the listing authority to impose sanctions on controlling shareholder for breach of duties, and second, the legislation[116] authorising the regulator to enforce the companies legislation has to be amended to permit enforcement of breaches of controlling shareholders' fiduciary duties.

III. Conclusion

Reforms have to be made to the private and public enforcement mechanisms so that breaches of controlling shareholders' fiduciary duties can be effectively enforced. The private enforcement mechanisms in the four countries in Asia can be significantly strengthened by simplifying and clarifying the law. Importantly, Singapore, Malaysia and Hong Kong should consider introducing a class action regime for derivative actions. Nevertheless, private enforcement is effective only insofar as the courts are effective and efficient. In India, unless and until the problem of inordinate delay afflicting the Indian courts is properly addressed, private enforcement is not a viable solution; the alternative is either arbitration or public enforcement.

Regarding public enforcement, among the four Asian countries, Hong Kong has arguably the best regime as the existing law expressly allows a public authority to address wrongs done to the company and shareholders. The other three countries should consider

[115] Bursa Malaysia LR, Chapter 15, LR 16.19(1)(b).

[116] Companies Commission of Malaysia Act 2001, s 17.

adopting this regime. If not, India's SEBI, and provided the necessary reforms are made, the regulators in Singapore and Malaysia can enforce breaches of controlling shareholders' fiduciary duties. Nevertheless, even if there are appropriate laws in place for public enforcement, what is equally important to bear in mind is the issue of inputs (i.e. the resources such as funding and staffing available to the regulator) and outputs (i.e. the number and types of enforcement actions and the sanctions imposed).[117]

Space constraint prevents the examination of two final issues. The first is whether the government as the controlling shareholder can be sued for breach of fiduciary duties. The short answer is that with the exception of the controlling shareholder of PRC state-owned enterprises in Hong Kong who enjoys crown immunity[118], the government as the controller in the SOEs in the other three Asian countries can be sued.[119] One suggested solution to get around the problem of PRC SOEs is to have the stock exchange in Hong Kong subject listed companies (which include PRC SOEs) to fiduciary duties and should there be any breaches, the companies and its directors should be subject to sanctions such as private or public warnings, fines, suspension of trading and possibly delisting.

The final issue concerns judicial independence, specifically, whether the courts in India, Malaysia and Singapore would be willing to rule against the government as the controlling shareholder and whether they will rule in an impartial manner when sensitive political issues are at stake.[120] A related issue concerns absence of corruption in the legislature, executive and

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[117] Howell E Jackson and Mark J Roe, 'Public and Private Enforcement of Securities Laws: Resource-based Evidence' (2009) 93 *Journal of Finance* 207.

[118] *Hua Tian Long* (No. 3) [2010] 3 HKC 557.

[119] Section 4(d), Singapore Government Proceedings Act (Cap 121); s 4(d) Malaysian Government Proceedings Act 1956; article 300, The Constitution of India (9 Nov 2015); *Nagendra Rao Case In N Nagendra Rao & Co. v State of AP* AIR 1994 SC 2663.

[120] See eg, HP Lee and Marilyn Pittard (eds), *Asia-Pacific Judiciaries: Independence, Impartiality and Integrity* (CUP 2017); Michael Safi, 'India's Top Judges Issue Unprecedented Warning Over Integrity of Supreme Court' *Guardian* (12 Jan 2018); Abhinav Chandrachud, 'The Insulation of India's Constitutional Judiciary' (2010) 45

judiciary in India and Malaysia[121] as this will affect the quality of enforcement by the public authorities and courts. Suffice to say that the effectiveness of enforcement depends not only on the laws and incentives related to enforcement – which have been analysed in this chapter – but also the integrity of public institutions.

Economic and Political Weekly 38; Austin Ramzy, 'Hong Kong's Courts Have Defended Its Freedoms. Is Beijing Changing That?' *New York Times* (5 Feb 2018).

[121] See eg World Justice Project Rule of Law Index 2017–2018 where the US, UK, Singapore, Hong Kong, Malaysia and India are ranked 19, 14, 4, 10, 44 and 67, respectively.

DPHIL CHAPTER 7: CONCLUSION

My central argument in this thesis is that controlling shareholders in the listed companies in the four common law jurisdictions in Asia should be subject to fiduciary duties. I have explained why the duties should be imposed, what the contents of the duties should be, by whom and how the duties can be imposed, as well as how the duties can be enforced.

Imposing fiduciary duties on controlling shareholders is not unprecedented (although the scope and operations in which the duties have been imposed in other jurisdictions differ from my thesis). For example, under US law, controlling shareholders owe the corporation a fiduciary duty to use their ability to control the corporation in a fair, just, and equitable manner.[1] They cannot exercise corporate powers for their own benefit.[2] While these fiduciary duties are usually imposed in the contexts of freeze-outs and private companies[3], it is not always the case.[4] Another example is that under German law, fiduciary duties are imposed on shareholders in general to prevent abuse of voting rights.[5] Shareholders are required to exercise these rights to promote corporate purpose.[6] The exercise of these rights contrary to corporate purpose or

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[1] *Jones v HF Ahmanson & Co* 460 P.2d 464 (Cal. 1969) 471.

[2] *Kavanaugh v Kavanaugh Knitting Co.*, 123 N.E. 148 (NY 1919).

[3] See eg, Melvin A Eisenberg, *Corporations and Other Business Organizations* (9th edn, Foundation Press 2005) 374, 678; Jesse H Choper and others, *Cases and Materials on Corporations* (7th edn, Wolters Kluwer 2008) 763, 957; William T Allen and Reiner Kraakman, *Commentaries and Cases on the Law of Business Organization* (5th edn, Wolters Kluwer 2016) 520-524.

[4] See eg, *Smith v At. Props., Inc.*, 422 N.E.2d 798 (Mass. App. Ct. 1981).

[5] Andreas Cahn, 'The Shareholders' Fiduciary Duty in German Company Law' in Hanne S Birkmose (ed), *Shareholders' Duties* (Wolters Kluwer 2017) 347-361.

[6] Ibid.

for purposes other than those stipulated by the company will contravene fiduciary duties.[7] Thus, a shareholder cannot exercise his voting right to benefit himself to the detriment of the company.

While the rationales for and the scope of the fiduciary duties, and the contexts in which they are imposed, vary in US law and German law, the important point is not that these laws should be uncritically transplanted to the four Asian countries. Rather, they should make us reconsider whether the current legal position in the four Asian countries (which is based largely on UK law) in which controlling shareholders are not subject to fiduciary duties is justifiable. It is also interesting to note that it has been argued that the US law on fiduciary duties should be extended to include activist minority shareholders (such as hedge funds) and to situations other than freeze-outs and closely-held companies.[8]

This brings me to the next point for consideration, namely, whether the analysis in this thesis has broader implication for the regulation of the conduct of other types of shareholders, specifically minority institutional shareholders in the listed companies in the four Asian jurisdictions, an issue of which requires further study. Minority institutional shareholders, especially hedge funds and state-owned enterprises, have interests that may conflict with the company and they may take actions that benefit themselves but are at the expense of the company and other shareholders. For example, while hedge fund activism is less common in the four Asian jurisdictions than the US and UK, there have been cases in which activist funds

[7] Ibid.

[8] See eg, Iman Anabtawi and Lynn Stout, 'Fiduciary Duties for Activist Shareholders' (2008) 60 *Stanford Law Review* 1255.

have pressurised companies in Hong Kong[9] (and Singapore[10]) to engage in share buybacks and to issue special dividends. Studies have shown that the abnormal share returns generated by hedge fund activism do not benefit the company or its stakeholders as they lead to wealth transfers from employees to shareholders, reductions in R&D expenditure and excessively risky investments.[11] Shareholder activism could result in the diversion of cash – that could be used to promote R&D, subsidise the prices of essential good such as life-saving drugs, or invest in the training of employees – to the current shareholders themselves.[12] Other than hedge funds, the interests of other types of institutional shareholders (such as mutual funds) can also conflict with the company because the former can vote in favour of the controlling shareholder to the detriment of the company because of the business relationships between the controller and the institutional investors.[13]

Regarding the government or state-owned enterprises, there are studies showing that the government institutional investor as a non-controlling shareholder sometimes provides

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[9] For eg, shortly after the US hedge fund, TCI Fund Management, disclosed its investment in Sinolink World Holdings, the board declared special dividends. Further, soon after Southeastern Asset Management, a US investment fund, publicly disclosed its investment in Great Eagles Holdings, the board declared special dividends. For further details, see Frank Wong, 'Shareholder Engagement and Activism Under the Radar: Empirical Evidence From Hong Kong (2003-15) — Rethinking Disclosure of Interests Regime' (23 June 2017) <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2725318> accessed 1 December 2018.

[10] Klaus Wille, 'New Singapore Activist Hedge Fund Seeks to Shake Up Companies' *Straits Times* (4 Feb 2015).

[11] See eg, Martijn Cremers and others, 'Short-Term Investors, Long-Term Investments, and Firm Value' (14 March 2017) <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2720248> accessed 1 December 2018; Yvan Allaire and François Dauphin, '"Activist" Hedge Funds: Creators of Lasting Wealth? What Do the Empirical Studies Really Say?' (Institute for Governance and Public Organizations, July 2014); Alon Brav and others, 'The Real Effects of Hedge Fund Activism: Productivity, Asset Allocation, and Labor Outcomes' (2015) 28 *Review of Financial Studies* 2723. Cf Alon Brav and others, 'Hedge Fund Activism, Corporate Governance, and Firm Performance' in William W Bratton and Jospeh McCahery, *Institutional Investor Activism: Hedge Funds and Private Equity, Economics ad Regulation* (OUP 2015) 261-304.

[12] John C Coffee Jr and Darius Palia, 'The Wolf at the Door: The Impact of Hedge Fund Activism on Corporate Governance' (2016) 1 *Annals of Corporate Governance* 1.

[13] Umakanth Varottil, 'The Advent of Shareholder Activism in India' (2012) 6 *Journal on Governance* 582, 593; Satatya Anand, 'Shareholder Activism in India' (2016) 4 *International Journal of Research in Humanities, Arts and Literature* 11, 13-14.

favours to their investee companies in return for personal gains or to pursue crony deals with the companies.[14] Thus, one question is whether minority institutional shareholders should also be subject to fiduciary duties, as their interests may conflict with those of the company.

Another reason for subjecting institutional shareholders to fiduciary duties does not relate to the regulation of conflict of interest but concerns giving effect to the stewardship codes in Singapore, Hong Kong and Malaysia. Under the codes, institutional shareholders are urged to promote and protect the long-term success of companies and to manage conflicts of interest.[15] The fundamental problem with these codes is that they are wholly voluntary and non-binding; no sanctions whatsoever are attached to non-compliance. One question is whether imposing fiduciary duties on institutional shareholders will not only facilitate the attainment of the codes' objectives, but also address the significant problem of passive institutional shareholders.[16]

Subjecting controlling shareholders and even institutional shareholders to fiduciary duties in the four Asian countries raises the bigger issue of the role of shareholders in these jurisdictions and the appropriate regulatory mechanisms. The literature on controlling shareholders is mainly concerned with the regulation of related party transactions (RPTs).[17]

[14] Aldo Musacchio and Sérgio G. Lazzarini, 'Leviathan in Business: Varieties of State Capitalism and Their Implications for Economic Performance' (May 30, 2012) 27-29, 40-41 <https://ssrn.com/abstract=2070942> accessed 1 December 2018; Anne O Krueger, 'Government Failures in Development' (1990) 4 *Journal of Economic Perspectives* 9; Mara Faccio, 'Politically Connected Firms' (2006) 96 *American Economic Review* 369, 384-385 (politicians extract rents from companies of which they are shareholders or directors).

[15] See eg, Singapore Stewardship Principles for Responsible Investors 2016, preamble, pg 3; Hong Kong Principles of Responsible Ownership 2016, para 6, pg 1.

[16] For evidence of domestic institutional shareholder passivity, see eg Umakanth Varottil, 'The Advent of Shareholder Activism in India' (2012) 6 *Journal on Governance* 582, 593; Jayati Sarkar and Subrata Sarkar, 'Large Shareholder Activism in Corporate Governance in Developing Countries: Evidence from India' (2000) 1 *International Review of Finance* 161; Mohammed Akbar Ali Khan, 'Corporate Governance and the Role of institutional Investors in India' (2006) 7 *Journal of Asia-Pacific Business* 37, 45-46.

[17] See eg, Lucas Enriques and others, 'Related Party Transactions' in Reiner Kraakman and others, *The Anatomy of Corporate Law: A Comparative and Functional Approach* (3rd edn, OUP 2017) Ch 6.

While this narrow focus is understandable given that RPTs are a persistent and pervasive means of extractions of private benefits of control by controllers, the broader issue of how other types of conflicts of interest which can also give rise to tunneling remains inadequately addressed. More importantly, this narrow focus on regulating RPTs does not give proper attention to the significant formal and informal powers wielded by controlling shareholders in concentrated ownership jurisdictions, and obscures a crucial, fundamental question, namely, for what purpose and for whose benefit controlling shareholders should exercise their powers. This explains in part why I have argued in this thesis that controlling shareholders should not only avoid authorised conflicts of interest, but should also act in good faith in the best interests of the company.

An implication of my thesis is that corporate governance may have to be reconsidered. Corporate governance is largely concerned with the powers and duties of the board of directors, including independent directors, in promoting and protecting shareholders' interests, and it has recently underscored the importance of increasing the powers of shareholders.[18] After all, a central legal and policy debate in the Anglo-American world since the early 20th century has been the 'agency' problem between board/management and the 'owners' (i.e. shareholders)[19], and the *ex ante* and *ex post* measures to address it. Seen in this light, regulating the powers of shareholders seems anomalous at best, and misguided at worst. But this view is lopsided. Shareholders, particularly controllers in concentrated ownership jurisdictions, play a critical role. In view of the significant powers that controlling shareholders wield and the conflicts of interest between them and the company, not only should their powers be regulated, but

[18] See eg, Marina Pargendler, 'The Corporate Governance Obsession' (2016) 42 *Journal of Corporation Law* 101.

[19] See eg, Reinier Kraakman and others, *The Anatomy of Corporate Law: A Comparative and Functional Approach* (3rd edn, OUP 2017) Ch 2-3.

controllers also have a responsibility to cooperate and collaborate with directors in order to promote corporate interest, which need not be equated with shareholders' or stakeholders' interests, but, rather, can refer to the long-term value and viability of the company.

In addition to controlling shareholders, institutional shareholders play an important role in corporate governance. Admittedly, the literature recognises the importance of institutional shareholders.[20] After all, reforms have been introduced to increase engagement by institutional shareholders[21] and much has been written about incentivising institutional shareholders to act on a long-term basis.[22] However, these measures do not address a deeper issue, namely, for what purpose and for whose benefit institutional shareholders should exercise their formal powers through voting and informal powers through pressure. My thesis may provide a tentative answer to this question. It is suggested that when institutional shareholders exercise corporate powers, or when the interests of institutional shareholders conflict with those of the company such that there is a risk that the company will take action that benefit these institutional investors but which is at the expense of the company and other shareholders, these institutional shareholders should be subject to fiduciary duties. This is not dissimilar to the case of controlling shareholders. Further, the analysis in my thesis concerning by whom and how the duties could be imposed as well as how the duties could be enforced will be relevant when

[20] OECD, The Role of Institutional Investors in Promoting Good Corporate Governance, Corporate Governance (2011).

[21] See eg, the stewardship codes in the UK, Singapore, Hong Kong and Malaysia; Directive (EU) 2017/828 of the European Parliament and of the Council of 17 May 2017 amending Directive 2007/36/EC as regards the Encouragement of Long-Term Shareholder Engagement; Iris H.-Y. Chiu, 'European Shareholder Rights Directive Proposals: A Critical Analysis in Mapping with the UK Stewardship Code?' (2016) 17 *ERA Forum* 31.

[22] See eg, Tamara Belinfanti, 'Shareholder Cultivation and New Governance' (2014) 38 *Delaware Journal of Corporate Law* 789 at 845 (suggesting weighted dividends dependent on length or quality of share ownership); Demetra Arsalidou, 'Shareholders and Corporate Scrutiny: The Role of the UK Stewardship Code' (2012) 9 *European Company and Financial Law Review* 342 at 376-77 (endorsing France's use of enhanced voting rights).

we consider the case of institutional shareholders. It is time to reconceptualise the role of shareholders in the four common law jurisdictions in Asia.

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