



# WMH Law Corporation

*Advocates & Solicitors*

12 Eu Tong Sen Street, #07-169, The Central, Singapore 059819

## Derivative Action by Shareholders

Civil Litigation Practice Series

Author's Details:-



**Mark LEE**

- Joint Managing Director
- Head of Corporate & Commercial Dispute Resolution Practice

HP: (+65) [9182 9643](tel:91829643)

Office: (+65) [6514 6352](tel:65146352)

Email: [mark.lee@wmhlaw.com.sg](mailto:mark.lee@wmhlaw.com.sg)

[www.wmhlaw.com.sg](http://www.wmhlaw.com.sg)

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**“Distinction between wrongs done to the company and a personal wrong suffered by a shareholder”**

# Derivative Action by Shareholders; Section 216A of the Companies Act

## Setting the Context

In our previous articles, we discussed the concept of the separate legal personality of a company and the different roles played by shareholders (owners) and directors (managers) within the company.

In this article, we discuss specific circumstance(s) where the shareholders may feel that the company ought to enforce certain corporate rights but its directors refuse to do so.

A common scenario is where the shareholders feel that the company ought to take a certain errant director to task but the Board of Directors (i.e. a “rogue” board) refuse to do so.

## Harm caused to the Company v. Loss suffered Personally by a Shareholder

In this instance, we touch on Section

216A of the Companies Act (Cap 50) (“the Act”); which provide shareholders the ability to **(1)** overcome an unwilling / uncooperative Board of Directors, **(2)** step into the shoes of the company **(3)** to right a corporate wrong committed against the company (**not** a wrong suffered in the shareholder’s *personal* capacity).

## The Proper Plaintiff Rule

The need for Section 216A of the Act is premised on the principle that “*in an action for a wrong alleged to have been done to a company (ie a corporate wrong) the proper plaintiff is prima facie the company itself.*” – i.e. the Proper Plaintiff Rule (**Ng Kek Wee v Sim City Technology Ltd** [2014] SGCA 47)

As such, Section 216A of the Act, provides an exception to the Proper Plaintiff Rule for shareholders to vindicate corporate wrongs.

## Statutory Derivative Action – Section 216A of the Act

Section 216A clearly sets forth certain “pre-requisites” that have to be satisfied before a statutory derivative action may be commenced. (**Petroships Investment Pte Ltd v Wealthplus Pte Ltd** [2016] SGCA 17) (“**Petroships Investment**”)

- a) A complainant must first apply to the High Court for leave / permission to bring a derivative action (Section 216A(2) of the Act).
- b) To do so, the complainant must have first given 14 days notice to the directors of the company of his / her intention to commence a derivative action. Simply, the directors of the company must first be given a chance to decide whether or not to vindicate the alleged corporate wrong (Section 216A(3)(a) of the Act).
- c) The Court must be satisfied that the complainant is “*acting in good faith*” (Section 216A(3)(b) of the Act). At the High Court level of **Petroships Investment**, the Judge accepted that a shareholder acted in good faith so long as its “*dominant purpose*” was to benefit the company.
- d) The Court must be satisfied that the complainant’s application is “*prima facie in the interests of the company*” (Section 216A(3)(c) of the Act).

Again, at the High Court level of **Petroships Investment**, the Judge stated that the question of whether a proposed derivative action was prima facie in the company’s interests involved not just an assessment of the legal merits of the action to determine if it was “*legitimate and arguable*” but also a holistic consideration of whether the action was in the “*practical and commercial interests of the company*”.

## Common Law Derivative Action

Whilst the issue of whether common law derivative actions “*co-exist with, or has been abrogated*” by the Act has not been conclusively determined, the High Court in **MCH International Pte Ltd v YG Group Pte Ltd** [2017] SGHCR 8 does provide the following guidelines to its application:-

- a) Procedural requirements – (i) A minority shareholder must bring an action on behalf of himself and all the other shareholders, excluding the majority wrongdoers; (ii) The wrongdoers must be named as defendants; (iii) The statement of claim must disclose that it is a derivative action.
- b) Substantive requirements – (i) The company has a reasonable case against the defendant; (ii) The plaintiff has locus standi to bring the action.

“Statutory Derivative Action v. Common Law Derivative Action”



**Derivative Action in the Context of Liquidation;**  
**(Petroships Investment Pte Ltd v Wealthplus Pte Ltd [2016]**  
SGCA)

In this case, for the first time, the Singapore Court of Appeal considered the question of whether shareholders of a company already in liquidation may commence a derivative action.

At the end of the Court of Appeal's analysis, it was decided that Section 216A of the Act is “*unavailable once a company is in liquidation.*” This includes a members' voluntary winding up.

Amongst other reasons, the Court of Appeal determined that Section 216A is “*intended to apply to companies other than those in the control of a liquidator.*” and also that the Act already provides statutory remedies in the liquidation regime

that “*negate the need for a shareholder to seek leave under*” Section 216A.

Significantly, the Court of Appeal also helpfully summarised the purpose of Section 216A;

“*The derivative action ... is one that avails a minority shareholder who is dissatisfied by the refusal of the board to act in the interests of the company. Its primary rationale is that it enables a party – who is aggrieved by the fact that those in control of the company are unwilling to act – to initiate the necessary legal action.*”



For more information on the article, or if you wish to learn more about the topics discussed, please contact:-

### **Mark LEE**

Joint Managing Director

HP: (+65) 9182 9643

Office: (+65) 6514 6352

Email: [mark.lee@wmhlaw.com.sg](mailto:mark.lee@wmhlaw.com.sg)

[www.wmhlaw.com.sg](http://www.wmhlaw.com.sg)

### **Wilbur LIM**

Joint Managing Director

HP: (+65) 9838 2910

Office: (+65) 6514 6351

Email: [wilbur.lim@wmhlaw.com.sg](mailto:wilbur.lim@wmhlaw.com.sg)

[www.wmhlaw.com.sg](http://www.wmhlaw.com.sg)

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