Re HL Sensecurity Pte Ltd (formerly known as HL Integral Systems Pte Ltd) [2006] SGHC 135

Case Number : CWU 198/2005

Decision Date : 31 July 2006

Tribunal/Court : High Court

Coram : Choo Han Teck J

Counsel Name(s) : Leslie Yeo Choon Hsien (Leslie Yeo & Associates) for the Company; Michael Moey Chon Woon (Moey & Yuen) for the Petitioner

Parties : —

Companies – Winding up – Whether company unable to pay its debts – Whether directors acting in the affairs of the company in their own interests rather than in the interests of the members as a whole – Whether just and equitable to wind up company – Sections 254(1)(e), 254(1)(f), 254(1)(i) Companies Act (Cap 50, 1994 Rev Ed)

31 July 2006

Choo Han Teck J:

1 This is a petition presented by Sensecurity Investments Pte Ltd for the winding-up of HL Sensecurity Pte Ltd ("the company"). The petition is premised upon the grounds stipulated in ss 254(1)(*e*), 254(1)(*f*) and 254(1)(*i*) of the Companies Act (Cap 50, 1994 Rev Ed), namely, that:

(a) The company is unable to pay its debt.

(b) The directors have acted in the affairs of the company in their own interests rather than in the interests of the members as a whole, or in any other manner whatever which appears to be unfair or unjust to the other members.

(c) It is just and equitable for the company to be wound up.

2 Having considered the arguments of the parties and the circumstances of the case, I was of the view that the company should be wound up based on ss 254(1)(*e*), 254(1)(*f*) and 254(1)(*i*) of the Companies Act, as the company was unable to pay its debts, because Charlie Ho had acted in a manner that was in his own interests rather than in the interests of the members as a whole and because it was just and equitable to do so.

Background facts

3 The company was formerly known as HL Integral Systems Pte Ltd and had two shareholders, Charlie Ho and Henry Ho. On 30 December 2002, the company entered into an agreement ("the agreement") with the petitioner for the sale and purchase of Sensecurity Pte Ltd ("Sensecurity"), which was a subsidiary of the petitioner, in consideration for the issuance of shares in the company to nominees of Sensecurity. Sensecurity's nominees were the petitioner, Infocomm Investment Pte Ltd ("Infocomm") and one Tan Lyn-Li. Under the agreement, the petitioner, Infocomm and Tan Lyn-Li were to hold 50% of the company's shares. Charlie and Henry Ho would hold the other 50% of the company's shares. The company was renamed as HL Sensecurity Pte Ltd to reflect its new shareholding.

4 A shareholders' agreement between the petitioner, Infocomm, Henry Ho and Charlie Ho was

entered into on 23 January 2003 ("the shareholders' agreement").Under the shareholders' agreement, the "A Shareholder" was defined to mean Charlie Ho and Henry Ho collectively and the "B Shareholder" was defined to collectively refer to the petitioner, Infocomm and Tan Lyn-Li.

5 Under cl 3.1 of the shareholders' agreement, A Shareholder was entitled to appoint five directors and B Shareholder was entitled to appoint seven directors to the board of directors of the company. Under cl 3.6 of the shareholders' agreement, no meeting of the Board could proceed to business unless a quorum was present at the start of the meeting, and that quorum had to consist of one director nominated by A Shareholder and one by B Shareholder. A meeting had to be adjourned if the quorum was not met, and only at the adjourned meeting could the quorum consist of any two directors.

6 Under cl 3.8 of the shareholders' agreement, a resolution of the Board was validly passed if the text of the resolution had been signed or approved by each director or his alternate. Under cl 4.1, matters requiring a supermajority vote of 75% of the total issued share capital included:

(a) the admission of any person or entity, whether by subscription for or transfer of shares, as a shareholder holding 5% or more of the issued share capital of the company;

(b) the opening or closing of any bank account; and

(c) changing the terms of the mandate of any bank account.

As a result of cl 4.1 of the agreement, there were two cheque signatories for the company, with one signatory nominated by A Shareholder and the other by B Shareholder. Representatives from A and B Shareholders were also given access to the company's internet banking facilities.

7 The five directors appointed by A Shareholder were Charlie Ho, Henry Ho, Wong Wai Leng, Low Eu Koon Jennifer and Tan Swee Giok. The seven directors appointed by B shareholder were Gene Ng Kean Gene, Low Jiunn Wei, Kenneth, Lewis Tan Liu Shen, Low Yih Wen, Christopher, Lee Fook Chiew, Brian, Cheng-Jean Chen (subsequently replaced by Tan Geok Leng) and Benjamin Gan Beng Chwee.

8 I now turn to consider each ground on which the petitioner relied in asking this court to wind up the company.

The company is unable to pay its debts

Allegations by the petitioner

9 According to the petitioner, the company had purchased software from Symantec Singapore Pte Ltd ("Symantec") on 19 September 2003 amounting to $2,240,890 for onward sale to the Ministry of Defence. The payments were to be made in 12 instalments. The company was to collect payments from the Ministry of Defence, deduct 2% for itself and forward the balance to Symantec.

10 For reasons unknown to the petitioner, the company became indebted to Symantec for the sum of US$550,000 as at 11 October 2005. This debt was in addition to the sum that was due to be paid to Symantec on 15 September 2005. The company then entered into an instalment plan to repay this debt.

11 Symantec's representative, one Alex Poon Tuck Wai ("Alex Poon"), gave evidence that the

company had defaulted on the instalment plan and now owes Symantec US$90,000. This figure does not take into consideration the instalment payments due after March 2006. Further, the company still owed Symantec $827,280 relating to the original payment plan for the deal involving the Ministry of Defence. These moneys remain outstanding despite the fact that the company had received payments from the Ministry of Defence. Symantec has demanded payment from the company.

Arguments by the respondent

12 The respondent company contended that it is not insolvent and that it will be able to repay the company's debts as and when they become due. In particular, Symantec, which is the company's main creditor, has agreed to a three-year plan which the company is presently servicing. Further, the company has reduced its expenses from a high of $110,580 per month in December 2004 to $24,197 per month in January 2006.

The relevant law

13 Section 254(1) of the Companies Act provides an exhaustive list of grounds on which the court may make an order for a company to be wound up. Under s 254(1)(*e*), winding-up may be granted if a company is unable to pay its debts. As a general rule, a company is insolvent when it cannot meet its obligations, actual or contingent, as and when they fall due. Additionally, s 254(2) provides a deeming provision for when a company is considered to be unable to pay its debts:

> **Definition of inability to pay debts.**
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> (2) A company shall be deemed to be unable to pay its debts if —
>
> (a) a creditor by assignment or otherwise to whom the company is indebted in a sum exceeding $10,000 then due has served on the company by leaving at the registered office a demand under his hand or under the hand of his agent thereunto lawfully authorised requiring the company to pay the sum so due, and the company has for 3 weeks thereafter neglected to pay the sum or to secure or compound for it to the reasonable satisfaction of the creditor;
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> (b) execution or other process issued on a judgment, decree or order of any court in favour of a creditor of the company is returned unsatisfied in whole or in part; or
>
> (c) *it is proved to the satisfaction of the Court that the company is unable to pay its debts; and in determining whether a company is unable to pay its debts the Court shall take into account the contingent and prospective liabilities of the company.*
>
> [emphasis added]

Findings of this court

14 Having assessed the evidence before me, I was of the view that the company was unable to pay its debts. In coming to this conclusion, I took note of the fact that the three-year instalment plan reached with Symantec was not for all outstanding debts, but only for debts owing before 15 September 2005.

15 Further, I accepted the petitioner's evidence that the company was using payments received from the Ministry of Defence to fund its own operations, rather than forwarding the moneys received

to Symantec. The company's balance sheet did not take into account the fact that the company still owed more than $800,000 to Symantec.

16 Additionally, the testimony of Alex Poon made clear that no agreement had been reached between Symantec and the company with regard to paying off the outstanding debts in one lump sum and those negotiations had been called off. Further, Alex Poon stated that as of January 2006, he was no longer confident that the company could repay its debts.

17 In these circumstances, I was of the view that the company should be wound up under s 254(1)(*e*) of the Companies Act.

Winding-up under s 254(1)(*f*) and 254(1)(*i*) of the Companies Act

18 Section 254(1)(*f*) of the Companies Act states that the court may order the winding-up of a company if:

> the directors have acted in the affairs of the company in their own interests rather than in the interests of the members as a whole, or in any other manner whatever which appears to be unfair or unjust to other members[.]

19 Section 254(1)(*i*) of the Companies Act states that the court may order winding-up if the court is of opinion that it is just and equitable that the company be wound up.

20 The petitioner combined its arguments under these provisions in support of its petition to wind up the company. Hence, I shall address them together.

Proposed management buyout

21 An extraordinary general meeting of shareholders of the company was held on 1 August 2005 to discuss a proposed management buyout of the company. Shareholders were presented with an undated letter from Charlie Ho supporting this proposal. This letter stated that the proposal had a number of advantages, including the fact that the current shareholders would be free from all concerns of the company including the raising of the funds that were required to keep the company afloat. The letter also indicated that if the company was wound up, it could lead to a review of the financial status and accounts of the company and to an investigation of whether there had been any irregularities.

Alleged deception by Charlie Ho

22 Charlie Ho sent an e-mail to shareholders on 3 December 2005, which stated that he had transferred all his shares to staff in the company and no longer had any shareholder interests. Further, Tan Swee Giok, Wong Wai Leng and Charlie Ho had resigned as directors of the company, and one Aisah Mahadi and one Adeline Wong were taking over. Aisah Mahadi was the finance manager of the company and Adeline Wong was Charlie Ho's sister-in-law. According to the petition, an Accounting & Corporate Regulatory Authority search on 7 February 2006 revealed that Charlie Ho never transferred his shares to his staff. To prevent this deception from being discovered, Charlie Ho instructed the company secretary to restrict the petitioner's access to inspect the company's books and documents.

Clauses 3.6, 3.8 and 4.1 of the shareholders' agreement

23 On 12 October 2005, the petitioner served a notice to the company and its shareholders to wind up the company. By this time, all the directors appointed by B Shareholder had resigned. As a consequence, the company called an extraordinary general meeting, to be held on 9 November 2005, to discuss, *inter alia*, the liquidation of the company. This resolution ended in a 50-50 deadlock. Further, the fact that Charlie Ho held 25.5% of the total number of issued shares meant that the company could never pass a resolution to liquidate the company since the supermajority of 75% of shareholders voting in favour of liquidation would never be achieved. Charlie Ho stated at this meeting that since there were no longer any directors who were representatives of B Shareholder, the term in the agreement requiring that a director nominated by B Shareholder should be present before there is quorum was void.

24 Additionally, Charlie Ho altered the mandate to the company's bank with regard to the cheque signatories to the company's account so that a signatory nominated by B Shareholder was no longer required.

Arguments by the respondent

25 The respondent contended that there was only one instance in which the shareholders were supposedly deadlocked, that being the extraordinary general meeting held on 9 November 2005. On that occasion, however, Tan Lyn-Li, who held 0.13% of the company's shares, was not present at the meeting. However, on the advice of the company's auditor, the vote in favour of winding-up was rounded up from 49.87% to 50%.

26 Additionally, the respondent argued that the petitioner could not argue that there was a deadlock since Infocomm and Tan Lyn-Li were not brought in as co-petitioners. Further, because cl 4 of the shareholders' agreement required a super majority of 75% of the votes to pass a resolution relating to voluntary liquidation of the company, the petitioner could not rely on the 9 November 2005 resolution to argue that there had been a shareholder deadlock.

27 With regard to the proposed management buyout, the respondent averred that Charlie Ho had simply been making a proposal that could be accepted or rejected by the shareholders. If the shareholders had rejected the proposal, as they in fact did, the proposal could not be carried out. Hence, there was no inequity arising from the proposal.

The relevant law

28 Section s 254(1)(*f*) of the Companies Act is seldom utilised in view of the provision's similarity with s 216 of the Companies Act. However, the relevant legal principles have been usefully summarised in *Foo Yin Shung v Foo Nyit Tse & Brothers Sdn Bhd* [1989] 2 MLJ 369. The provision has two limbs, the first containing the phrase "interests of the members as a whole" and the second, the phrase "unfair and unjust to other members". The former phrase was interpreted in *Re Cumberland Holdings Ltd* (1976) 1 ACLR 361 to mean a situation where directors are shown to have preferred their own interest to the interests of one, or more or perhaps some significant section of the members so that the action of the directors may be open to challenge. The provision applies when the directors are seen not to have been acting in the interests of all the members and cannot therefore be said to be acting in the interests of the members as a whole. Hence, the scope of the provision is very wide. With regard to the latter phrase, the words "unfair and unjust" have reference to commercial morality or integrity which the law ought to uphold or sustain, having regard to all the circumstances.

29 The principles governing the application of the just and equitable ground of winding up a company under s 254(1)(*i*) of the Companies Act have received comprehensive treatment in the

recent Court of Appeal case of *Sim Yong Kim v Evenstar Investments Pte Ltd* [2006] SGCA 23 ("*Evenstar*"). In *Evenstar*, Chan Sek Keong CJ expressly approved Lord Wilbeforce's exposition on the meaning of "just and equitable" in *Ebrahimi v Westbourne Galleries Ltd* [1973] AC 360 ("*Ebrahimi*"). Lord Wilberforce's discussion was in the context of the former s 222(f) of the Companies Act 1948 (c 38) (UK) (presently s 122(1)(g) of the Insolvency Act 1986 (c 45) (UK)), which is the equivalent of our s 254(1)(*i*) of the Companies Act, and his Lordship stated as follows at 379–380:

> The words [just and equitable] are a recognition of the fact that a limited company is more than a mere legal entity, with a personality in law of its own: that there is room in company law for recognition of the fact that behind it, or amongst it, there are individuals, with rights, expectations and obligations inter se which are not necessarily submerged in the company structure. … The "just and equitable" provision does not, as the respondents suggest, entitle one party to disregard the obligation he assumes by entering a company, nor the court to dispense him from it. It does, as equity always does, enable the court to subject the exercise of legal rights to equitable considerations; considerations, that is, of a personal character arising between one individual and another, which may make it unjust, or inequitable, to insist on legal rights, or to exercise them in a particular way.
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> *It would be impossible, and wholly undesirable, to define the circumstances in which these considerations may arise*. Certainly the fact that a company is a small one, or a private company, is not enough. There are very many of these where the association is a purely commercial one, of which it can safely be said that the basis of association is adequately and exhaustively laid down in the articles. The superimposition of equitable considerations requires something more, which typically may include one, or probably more, of the following elements: (i) an association formed or continued on the basis of a personal relationship, involving mutual confidence – this element will often be found where a pre-existing partnership has been converted into a limited company; (ii) an agreement, or understanding, that all, or some (for there may be "sleeping" members), of the shareholders shall participate in the conduct of the business; (iii) restriction upon the transfer of the members' interest in the company – so that if confidence is lost, or one member is removed from management, he cannot take out his stake and go elsewhere.
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> It is these, and analogous, factors which may bring into play the just and equitable clause, and they do so directly, through the force of the words themselves. To refer, as so many of the cases do, to "quasi-partnerships" or "in substance partnerships" may be convenient but may also be confusing. *It may be convenient because it is the law of partnership which has developed the conceptions of probity, good faith and mutual confidence, and the remedies where these are absent, which become relevant once such factors as I have mentioned are found to exist: the words "just and equitable" sums these up in the law of partnership itself*. And in many, but not necessarily all, cases there has been a pre-existing partnership the obligations of which it is reasonable to suppose continue to underlie the new company structure. But the expressions may be confusing if they obscure, or deny, the fact that the parties (possibly former partners) are now co-members in a company, who have accepted, in law, new obligations. A company, however small, however domestic, is a company not a partnership or even a quasi-partnership and it is through the just and equitable clause that obligations, common to partnership relations, may come in.
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> [emphasis added]

30 Chan CJ went on to state at [31] of *Evenstar* that the notion of unfairness lies at the heart of the "just and equitable" jurisdiction in s 254(1)(*i*) of the Companies Act. An unhappy member of a

company cannot use the clause to escape at will, nor can it be utilised where the loss of trust and confidence has been self-induced. Significantly, Chan CJ opined that:

> Cases involving management deadlock or loss of mutual trust and confidence where the "just and equitable" jurisdiction under s 254(1)(*i*) has been successfully invoked can be re-characterised as cases of unfairness, whether arising from broken promises or disregard for the interests of the minority shareholder.

Findings of this court

31 It should first be noted that I found nothing inequitable about the proposed management buyout. Although the proposal had been on terms dictated by Charlie Ho, the shareholders were free to accept or reject it. When the shareholders did, as a matter of fact, reject the proposal, Charlie Ho could not implement it and his purported takeover bid failed.

32 However, Charlie Ho had deliberately breached the agreement in altering the mandate to the company's bank with regard to the cheque signatories to the company's account so that B Shareholder's signatory was no longer required. He had also acted in his interests rather than the interests of the shareholders by lying about having transferred his shares in the company to the staff of the company. This was a deliberate untruth that was aimed at facilitating his takeover of the company. In these circumstances, I was of the view that the petitioner's case under s 254(1)(*f*) of the Companies Act had been made out and the company could be wound up on this basis.

33 Turning next to the arguments relating to s 254(1)(*i*) of the Companies Act, when the partnership between Charlie Ho and Henry Ho on one hand, and the petitioner, Infocomm and Tan Lyn-Li on the other, was first formed, it was clearly contemplated that both groups would be equal share partners in the collective enterprise. Neither A Shareholder nor B Shareholder was envisaged as having the dominant shareholding or the majority vote in the company. The management and operational decisions of the company were to be decided jointly. Further, it is clear that, given the breakdown in the relationship between A Shareholder and B Shareholder, the company cannot continue to function since management decisions will always be deadlocked and the company cannot move ahead. Evidence for this can be derived from the fact that even though Tan Lyn-Li was not present at the meeting on 9 November 2005, the company's auditor saw fit to round up the vote against the resolution to 50%. It was clear how Tan Lyn-Li was going to vote.

34 Accordingly, it was clear that it would also have been just and equitable to wind up the company on the basis that the company could not continue with its affairs due to the breakdown in relationship between the two groups of shareholders. For the reasons above, I ordered that the company to be wound up with the consequential orders as agreed by the parties in terms of their draft consent order dated 4 July 2006.