

ENFORCING CORPORATE DISCLOSURE

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This article suggests that the gist of securities market disclosure is the furtherance of corporate governance and not investor protection. It will be argued that public enforcement of continuous disclosure rules remains the primary means of enforcement in Singapore. But this should be supplemented by private enforcement. While jurisdictions like the U.K. have introduced legislation loosely mirroring 10b-5 actions in the U.S., allowing investors to seek compensation largely from issuers (and their insurers), recent literature suggests this is a suboptimal solution, given that any damages are ultimately borne by existing shareholders. Courts also face difficulties in conceptualising or quantifying shareholder losses since these are derived from information concerning the assets and prospects of the underlying company. But Singapore courts have shown that it is possible to treat corporate misstatements as a form of fraud against the entity, where generous causation and remoteness rules are available to measure the damages suffered by the corporation.

I. CONTINUOUS DISCLOSURE: PUBLIC AND PRIVATE ENFORCEMENT

Investors take the risk of poor management and this is usually not something for the courts to decide but for investment analysts to pick up, and investors to inform themselves about.¹ In the more egregious cases, however, directors may be sued for wrongdoing, including negligence, although investors would find it hard to succeed² or even to have standing to commence an action. The proper plaintiff in such cases is usually the company, unless a shareholder can show that a duty of care was owed to him or her due to a special circumstance. Does or should that special circumstance exist at common law where corporate disclosure is concerned, or is it something that is implicitly recognised in the relevant statutory provisions in Singapore such as

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¹ Zohar Goshen & Gideon Parchomovsky, “The Essential Role of Securities Regulation” (2006) 55 Duke L.J. 711.

² While we do not have a formal business judgment rule in Singapore, in *ECRC Land Pte. Ltd. v. Wing On Ho Christopher* [2004] 1 S.L.R. 105, Tay Yong Kwang J. held that courts do not second-guess the commercial decisions of directors acting in the best interests of the company. Compare V.K. Rajah J.C. (as he then was) in the later decision of *Vita Health Laboratories Pte. Ltd. v. Pang Seng Meng* [2004] 4 S.L.R. 162 (H.C.) [*Vita Health*]. See also *Vines v. Australian Securities & Investments Commission* (2008) 62 A.C.S.R. 1 (N.S.W.C.A.) for an example of the context-specific way in which the statutory duty of care and skill has been applied in Australia.

sections 199 (which punishes the maker of false and misleading statements that are likely to induce the subscription of or sale or purchase of securities, or which are likely to affect the market price of securities) and 203 (which targets the issuer corporation for breaches of an exchange's continuous disclosure rules) of the *Securities and Futures Act*?³ If so, is it or should it be a duty to care or a duty to take care?

Paul Davies has said in the context of his review of the present corporate disclosure regime in the U.K. implementing the European Union *Transparency Directive (E.U.)*, however, that he is “persuaded by the arguments which put the weight of enforcement burden on public rather than private actors and confine private enforcement to the area of fraudulent claims.”⁴ There should therefore always be a criminal backstop at the top of the regulatory pyramid.⁵ In Singapore, market misconduct, which includes sections 199 and 203, is backed by criminal sanctions found in section 204 of the *Securities and Futures Act (Singapore)*.⁶ In the U.K., there is the market abuse regime in the *Financial Services and Markets Act 2000 (U.K.)* under which the Financial Services Authority may impose unlimited fines.⁷ Alongside that is section 91(1B) of the *Financial Services and Markets Act 2000 (U.K.)* which was introduced pursuant to the *Transparency Directive (E.U.)* that, read with section 382, allows the Financial Services Authority to obtain a civil penalty and restitution. These hybrid actions are found in Singapore under section 232 of the *Securities and Futures Act (Singapore)* and the new section 236L, introduced by the *Securities and Futures (Amendment) Act 2009*. The latter allows disgorgement of whole or part of a benefit received by a third party on application of the Monetary Authority of Singapore (“MAS”) or a person who has suffered loss as a result of market misconduct.

It should be observed, though, that the strongest advocates of the “law matters” school in other areas of company law believe that what matters most is that securities laws facilitate enforcement by private actors, rather than public enforcement.⁸

³ Cap. 289, 2006 Rev. Ed. Sing. [*Securities and Futures Act (Singapore)*].

⁴ Paul Davies Q.C., *Davies Review of Issuer Liability: Final Report* (June 2007), online: <http://www.hm-treasury.gov.uk/d/davies_review_finalreport_040607.pdf> at para. 18 [*Final Report*]. His recommendations were accepted by the U.K. Government: H.M. Treasury, *Extension of the statutory regime for issuer liability* (July 2008), online: <http://www.hm-treasury.gov.uk/d/issuerliability_170708.pdf> [*H.M. Treasury*].

⁵ Ian Ayres & John Braithwaite, *Responsive Regulation: Transcending the Deregulation Debate* (New York: Oxford University Press, 1992), and applied by the Australian Treasury in their Consultation Paper, *Review of Sanctions in Corporate Law* (March 2007), online: <http://www.treasury.gov.au/documents/1182/PDF/Review_of_Sanctions.pdf>. See also George Gilligan, Helen Bird & Ian Ramsay, *Regulating Directors' Duties—How Effective are the Civil Penalty Sanctions in the Australian Corporations Law?*, Centre for Corporate Law and Securities Regulation, University of Melbourne (1999), online: <<http://cclsr.law.unimelb.edu.au/research-papers/Monograph%20Series/Civil%20Penalties%20Final.pdf>> at 8.

⁶ The criminal sanctions for the market misconduct provisions in the *Securities and Futures Act (Singapore)*, Part XII are a fine of up to \$250,000 and imprisonment of up to 7 years.

⁷ *Financial Services and Markets Act 2000 (U.K.)*, Part 8, especially s. 118, and also s. 397. The *Market Abuse Directive (E.U.)* came into force on 1 July 2005. The Financial Services and Markets Tribunal confirmed in the prosecution of Paul Davidson that market abuse is criminal in nature: see *International Financial Law Review*, (July 2006) at 8. So, although the burden of proof is the civil “balance of probabilities”, the Tribunal thought that the seriousness of market abuse meant that the standard of proof was no different from the criminal one.

⁸ Rafael La Porta, Florencio Lopez de Silanes & Andrei Shleifer, “What Works in Securities Laws?” (2006) 61 *J. Fin.* 1.

More recently, others have provided some empirical evidence to show that public enforcement can be just as useful as disclosure, and more important than private enforcement, in deepening financial markets.⁹ In a small economy like Singapore's, in particular, it may be that the MAS, through the use of civil penalties, is the most cost efficient and effective enforcer of securities laws rather than the investors themselves or any self-regulatory organisation.¹⁰ Similarly, in Hong Kong, the Market Misconduct Tribunal hears cases by their regulators for civil penalties.¹¹ This is likely to be the case even in larger Asian countries due to the less developed nature of their securities markets and enforcement mechanisms.¹²

There is, however, always the possibility of regulatory capture. In Australia, where empirical evidence has shown that the main mode of enforcement is still by the Australian Securities and Investments Commission ("ASIC"),¹³ there was a recent instance where Telstra ignored an infringement notice served on it by ASIC, and the latter did not then bring a civil penalty action against it.¹⁴ And Securities and Exchange Commission ("SEC") actions in the U.S. against individual wrongdoers and issuers in cases of corporate disclosure which, as we will see, serves a greater deterrence function than class actions by investors against issuers for compensation,

⁹ Howell E. Jackson & Mark J. Roe, "Public and Private Enforcement of Securities Laws: Resource-Based Evidence" (16 March 2009) Harvard Public Law Working Paper No. 08-28; Harvard Law and Economics Discussion Paper No. 638, online: <<http://ssrn.com/abstract=1000086>>.

¹⁰ Eliot Spitzer, the former Attorney-General for New York, in Congressional hearings has stated that self regulatory organisations have been an "abject failure": U.S. House of Representatives, Sub-committee on Capital Markets, Insurance and Government-Sponsored Enterprises, Committee on Financial Services, *Mutual Funds: Who's Looking Out for Investors* (4 November 2003), online: <<http://www.access.gpo.gov/congress/house/pdf/108hr92982.pdf>>.

¹¹ The Hong Kong Securities and Futures Commission have also obtained 10 convictions with 7 sentences of imprisonment since July 2008.

¹² For example, a China Supreme People's Court circular in 2001 on civil compensation claims in securities frauds stated that "the people's courts do not have adequate resources to accept and hear such cases due to current legislative and judicial limitations": see Shi Chenxia, "The Recent Rules of the Supreme People's Court of the P.R.C on Handling Cases Concerning Information Disclosure of Listed Companies" [2008] 26 C. & S.L.J. 344. In later circulars, the Supreme People's Court allowed courts to hear such actions if the company had been administratively sanctioned for false disclosure by China Securities Regulatory Commission or other administrative agencies or been criminally convicted. This suggests that the primary action is still taken by the regulator and investors might then piggy-back on that action, which is the case in Singapore under the *Securities and Futures Act (Singapore)*, s. 234, discussed below at Part III. The only exception appears to be in Taiwan where Taiwan's Securities and Futures Investor Protection Centre listens to investor complaints and files class action lawsuits for investor compensation, which is similar to what the Australian Securities and Investments Commission does under the *Australian Securities and Investments Act (Cth)*, s. 50. Under this provision, the Australian Securities and Investments Commission can take over an action on behalf of investors. However, Janet Austin, "Does the Wespoint litigation signal a revival of the ASIC s 50 class action?" (2008) 22 *Austl. J. Corp. L.* 8 at 23 points out that the legislative history, and particularly the need to prove that the action is in the public interest, shows that it is the regulatory motive, rather than compensation, that is the driving force behind its use.

¹³ Helen Bird, *et al.*, "ASIC Enforcement Patterns, Centre for Corporate Law and Securities Regulation, University of Melbourne (2003), online: <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=530383> at 107. See now Elizabeth Boros, "Public and Private Enforcement of Disclosure Breaches in Australia" [2009] 9 J.C.L.S. 409 [*Public and Private Enforcement*].

¹⁴ Marina Nehme, Margaret Hyland & Michael Adams, "Enforcement of Continuous Disclosure: The use of infringement notice and alternative sanctions" (2007) 21 *Austl. J. Corp. L.* 112 at 125-126.

have faced problems with funding.¹⁵ It was the late Professor Galbraith that said that regulators were “[v]igorous in youth, rapidly turning complacent in middle age, before either becoming senile or an arm of the industry they are meant to regulate.” In any case, it is not immediately obvious why wealth should be shifted from shareholders to the regulators which is the case particularly in a treble civil penalties regime such as exists in section 232 of the *Securities and Futures Act (Singapore)* that we shall see serves, alongside criminal actions, as the only enforcement mechanisms in Singapore. Regulators in the U.K. have also had problems with the high burden of proof in obtaining civil penalties for market abuse,¹⁶ and in Australia, the ASIC may not know what matters will be raised by the defence as the court does not order discovery in such actions.¹⁷ In Singapore, there have also been problems enforcing judgments for civil penalties obtained in foreign jurisdictions.¹⁸

Still, there should be a necessary range of sanctions with the public ones at the top and private enforcement lower down the hierarchy, but with the caveat that this should mainly be by the issuer corporation against the wrongdoers that create fraudulent disclosures, rather than by shareholders against those wrongdoers or, which is usually the case in the U.S. under their 10b-5 securities fraud actions, and now expressly provided in the U.K. in section 90A of the *Financial Services and Markets Act 2000 (U.K.)* (introduced pursuant to the *Transparency Directive (E.U.)* and commencing on Royal Assent, 8 November 2006) against the issuer corporation. Investors should have no right of action except exceptionally, such as in the case where a board sends them a takeover circular that is intended for their consideration and action.¹⁹ Thus,

¹⁵ See Merritt Fox, “Why Civil Liability for Disclosure Violations When Issuers Do Not Trade?” (2009) Wis. L. Rev. 297 at 319 [*Why Civil Liability for Disclosure Violations*]. At 332 he points out that the legislature may envisage vibrant private enforcement as it sees future limitations on public enforcement for special interest or political reasons. But this may be less a practical matter than a philosophical one; at 329, he argues that there is a view that “the public-enforcement budget is making up for a shortfall of private enforcement, not private enforcement making up for a shortfall in the public-enforcement budget.” See now Donald C. Langevoort, “The SEC and the Madoff Scandal: Three Narratives in Search of a Story” (18 September 2009). Georgetown Law and Economics Research Paper No. 1475433; Georgetown Public Law Research Paper No. 1475433, online: <<http://ssrn.com/abstract=1475433>> (discussing the “relative poverty” of the SEC at 15-16).

¹⁶ See *supra* note 7. This may be a result of the quasi-criminal nature of market abuse, and may not be the case with breaches of the *Disclosure Rules* and *Transparency Rules* of the U.K. Listing Authority.

¹⁷ See Austin, *supra* note 12 at 20.

¹⁸ Although the *Securities and Futures Act (Singapore)* states clearly that the civil burden of proof applies in the case of ss. 232 and 234, these provisions may still be seen as criminal in nature by a foreign court enforcing the action, which is how the Singapore court classified a U.S. Securities Exchange Commission civil penalty action for insider trading in *Securities Exchange Commission v. Bobby Ong* [1999] 1 S.L.R. 310 (H.C.).

¹⁹ Davies, *Final Report*, *supra* note 4 at para. 44, which is consistent with his earlier academic work: Paul Davies, “Directors’ Fiduciary Duties and Individual Shareholders” in Ewan McKendrick, ed., *Commercial Aspects of Trusts and Fiduciary Obligations* (New York: Oxford University Press, 1993) 83 at 114. But even in these takeover cases there are issues of causation. Often, it is only where the wrongdoer makes a profit that we are comfortable allowing investor compensation. So in *Re Austral Coal Ltd.* (No. 2) [2005] A.T.P. 20, the Australian Takeover Panel only disgorged gains (or loss avoided through paying a lower price) where a substantial shareholding was acquired without the necessary disclosures. Such an approach reinforces Dawson’s “rudimentary psychology” that “loss alone is a grievance. But if this loss can be located and identified in the gain received by another, the anguish caused by the loss will be felt as more than double”: John P. Dawson, *Unjust Enrichment: A Comparative Analysis* (Boston: Little, Brown & Co, 1951) at 5. The U.K. takeover situation is different as the Takeover Panel is now under the *Companies Act 2006 (U.K.)*, s. 954 empowered to obtain compensation for breach of a rule

according to Merritt Fox, a leading commentator on corporate disclosure in the U.S., “[t]he moment is ripe for a fundamental re-evaluation of how to design a system of civil liability for mandatory securities disclosure violations.”²⁰

II. CONTINUOUS DISCLOSURE: CORPORATE GOVERNANCE OR INVESTOR PROTECTION²¹

While disclosure is a management decision, it seems to be qualitatively different from, say, a decision whether to invest in new plant or equipment. Disclosure is described by Zohar Goshen and Gideon Parchomovsky as one of the three pillars of securities regulation, alongside restrictions on fraud and manipulation, and proscriptions on insider trading. This creates a competitive market for analysts or professional investors, which in turn helps police against breaches of the duty of care on the part of directors.²² So disclosure has a crucial role in market efficiency as well as corporate governance,²³ which is sometimes lost in the powerful rhetoric of investor protection. For example, investor protection is the first of three general objectives in securities regulation expounded by the International Organisation of Securities Commissions (“IOSCO”).²⁴ Countries such as Australia and the United Kingdom have adopted the three IOSCO objectives without modification.

In Singapore, however, investor protection is not mentioned as one of the objectives of market regulation in section 5 of the *Securities and Futures Act (Singapore)*, which was introduced by the *Securities and Futures (Amendment) Act 2005*, and has in its place the objective of facilitating “efficient markets for the allocation of capital and the transfer of risks.” Consequently, ensuring that markets are “fair, orderly and transparent”, which was largely the second IOSCO objective, but listed first in section 5(a) of the *Securities and Futures Act (Singapore)*, appears to be the primary objective in Singapore.²⁵ However, the move towards a disclosure-based regime must not be seen as a fundamental shift in philosophy—it should be recognised that the disclosure philosophy has permeated securities regulation in Singapore to varying degrees since at least 1974. In that year, it was said by the then Minister for Finance, Mr. Hon Sui Sen, at the Second Reading of the *Companies (Amendment) Bill*, that “[d]isclosure of information is an essential part of the working of a free

the effect of which is to require the payment of money. But both show the need for clear definition of claimable amount, which is the problem an investor claimant faces under the *Securities and Futures Act (Singapore)*, s. 234: see Part III below.

²⁰ Merritt Fox, “Civil Liability and Mandatory Disclosure” (2009) 109 Colum. L. Rev. 237 at 240 [*Civil Liability and Mandatory Disclosure*].

²¹ It could, of course, be neither: see generally, Frank H. Easterbrook & Daniel R. Fischel, “Mandatory Disclosure and the Protection of Investors” (1984) 70 Va. L. Rev. 669 at 671.

²² Goshen & Parchomovsky, *supra* note 1.

²³ Fox, *Civil Liability and Mandatory Disclosure*, *supra* note 20 at Part II.

²⁴ See International Organization of Securities Commissions (IOSCO), *Objectives and Principles of Securities Regulation* (May 2003), online: <<http://www.legco.gov.hk/yr04-05/english/panels/fa/papers/fa0217cb1-880-9e.pdf>>, where 30 principles are based on the three objectives, with the second being to “promote fair, efficient and transparent markets” which is in the *Securities and Futures Act (Singapore)*, s. 5(a) as “fair, orderly and transparent” and the third “to reduce systemic risk” which is in s. 5(c).

²⁵ These objectives are discussed in greater detail in the Monetary Authority of Singapore, “Securities and Futures Act (Cap 289): Guidelines on the Regulation of Markets” (1 July 2005), online: <http://www.mas.gov.sg/masmcm/bin/pt1SFA_Guidelines.htm>.

and fair economic system, subject to certain limitations to allow for competitive situations.”²⁶

What may be different from other jurisdictions is that the re-emphasis on the disclosure-based approach at the start of this decade was expressly associated with a *caveat emptor* philosophy. The then Deputy Prime Minister, Mr. Lee Hsien Loong, said during the second reading of the *Securities and Futures Bill 2001* (Bill 33 of 2001):

The public will be reminded time and again that the primary responsibility for making investment decisions lies with themselves and, over time, they will be able to learn to be able to look out for their own interest. There is no alternative. We have to shift. We cannot go on the basis that the regulator, or MAS, or the [Singapore Exchange] will make sure that every investment is safe and sure to make money. If you want to invest, you have to make your own judgment, find out your own information and make your own decisions.²⁷

In contrast, in its introduction in the U.S. by the *Securities Act 1933 (U.S.)*, President Roosevelt spoke in support of the disclosure philosophy by stating that “[t]his proposal adds to the ancient rule of caveat emptor [‘Let the buyer beware’] the further doctrine: ‘Let the seller also beware’ [caveat venditor]. It puts the burden of telling the whole truth on the seller.” While the 1933 Act focused on the primary market, the *Transparency Directive (E.U.)* (which focus is on continuous disclosure) recitals state quite clearly that disclosure is for investor protection.²⁸

In Singapore, however, the corporate governance basis for continuous disclosure was emphasised in an important sentencing decision, for which the defendant pleaded guilty to breaches of sections 199 and 203 of the *Securities and Futures Act (Singapore)* (amongst other offences). In *Public Prosecutor v. Chen Jiulin*,²⁹ the facts of which are discussed below,³⁰ the Court made the following observation:

As a general sentencing consideration, it is well accepted that our securities market is market driven, and subscribes to a disclosure-based regulatory regime. Encouraging good corporate governance is vital to the integrity, efficiency and transparency of our securities market as well as for the protection of investors. Timely corporate disclosure is an essential feature of our corporate governance. Market manipulation, false trading and the making of false statements severely distort the true nature of the market. Such actions are viewed seriously

²⁶ Sing., *Parliamentary Debates*, vol. 33 at col. 956 (27 March 1974). Although the first *Securities Industry Act* was only introduced in 1973, informal regulation of the markets existed before that: see Hans Tjio, *Principles and Practice of Securities Regulation in Singapore* (Singapore: LexisNexis, 2004) at [2.01].

²⁷ Sing., *Parliamentary Debates*, vol. 73 at col. 2162 (5 October 2001).

²⁸ E.g., *Transparency Directive (E.U.)*, recital (4) states that “[g]reater harmonisation of provisions of national law on periodic and ongoing information requirements for security issuers should lead to a high level of investor protection throughout the Community.” See further the U.K. Financial Markets Law Committee, *Issue 76 – Transparency Obligations Directive* (October 2004), online: <<http://www.fmlc.org/papers/fmlc76oct12.pdf>> at para. 3.7.

²⁹ D.A.C. 23249/2005, details of which are gleaned from *Public Prosecutor v. Tan Hor Peow Victor* [2006] SGDC 148 [*Tan Hor Peow Victor*] and *Public Prosecutor v. Wang Ziyi Able* [2007] SGHC 204 (discussed by Toh Yung Cheong, “Knowing, Not Knowing and Almost Knowing” (2008) 20 S.Ac.L.J. 677) and Chew Heng Ching *et al.*, *Casebook on Corporate Governance* (Singapore: Sweet & Maxwell Asia, 2009) Case Study 9.

³⁰ See *infra* note 36 *et seq.* and accompanying text.

III. SINGAPORE POSITION

Section 203 of the *Securities and Futures Act (Singapore)*, which came into being with the passing of that piece of legislation in 2002, creates what in Singapore is the main regulatory offence for breaching the continuous disclosure rules of a securities exchange. Liability is triggered by intentional, reckless or (in the case of civil penalties and compensatory claims only) negligent behaviour. Under section 232, the MAS may seek to obtain civil penalties amounting to three times the amount of the profit made or loss avoided by the contravening person, which in the case of section 203 is the issuer corporation. Where no such profit is made or loss avoided, which is usually the case in a failure by an issuer to satisfy the continuous disclosure requirements in section 203, the MAS is empowered to obtain up to \$2 million as a civil fine.³¹ For investors, section 234 permits all persons suffering a loss while trading contemporaneously with a contravening person to recover a 'maximum recoverable amount' from the contravening person, which is the amount of profit made or loss avoided by the contravening person. If a court, utilising the guidelines on the meaning of contemporaneity,³² finds that there are numerous such investors, each of them will not recover a substantial amount based on the statutory limit. But in any case, since the contravening person for the purposes of the continuous disclosure rule in section 203 is the issuer company itself, which may not have made a profit or avoided a loss from failure to disclose material information unless it was also issuing new shares at the same time, investors will usually be unable to recover anything at all. This has been criticised by a number of academics in Singapore, as has the fact that there is no presumption of reliance or fraud on the market concept to help with the formation of securities class actions.³³ But it is consistent with a weak investor protection philosophy in Singapore.

Section 199, which prohibits a person from making false statements that are likely to affect the trading of securities or their market price, however, attributes liability to the maker of the statement, which could be the corporation in cases of periodic financial statements, or an individual officer or director making a specific disclosure on behalf of the entity. In the former case, any claim under section 234 by investors would face the same concomitant problems as above. There have, however, been instances where an individual has clearly made misstatements on behalf of the company,³⁴ or has had a corporate misstatement attributed to it under section 331 of

³¹ See Aedit Abdullah *et al.*, "A Practical Guide to Quantifying Civil Penalties under the SFA" Singapore Law Gazette (November 2004).

³² See Tan Cheng Han, "Protecting the Integrity of the Securities Market: Recent Amendments to the Law Relating to Insider Trading" [2000] Sing. J.L.S. 33.

³³ Wan Wai Yee, "Civil Liabilities for False or Misleading Statements Made by Listed Companies to the Securities Market in Singapore" (2008) 26 C. & S.L.J. 377; Alexander Loke, "The Efficacy of Securities Investors' Rights in Singapore" [2009] Sing. J.L.S. 109 [*Efficacy of Securities Investors' Rights in Singapore*]. See also Joyce Lee, "'Americanisation' of the civil liability regime for insider trading in Singapore" (2005) 23 C. & S.L.J. 396.

³⁴ Chen also made false statements while commenting on the financial statements of China Aviation Oil: see the class action filed in the Southern District of New York in *Leong Yan Thieng v. China Aviation Oil (Singapore) Corp Ltd.* (S.D.N.Y.), online: <http://securities.stanford.edu/1033/CAOLFPK05_01/2005210_o01c_0502018.pdf>. But he was fined under a combination of *Securities and Futures Act (Singapore)*, ss. 199(c)(i) and 331, *i.e.*, corporate liability from which was derived individual liability, rather than direct individual liability.

the *Securities and Futures Act (Singapore)*. This latter provision imposes criminal liability on an officer of a body corporate where an *offence* has been created by a body corporate which “is proved to have been committed with the consent or connivance of, or to be attributable to any neglect on the part” of the officer. But where direct, as opposed to derived, individual liability is concerned, it will be seen below that it is still possible to impose such liability on the individual where the standard of liability in section 199 is recklessness, a subjective standard, as opposed to the objectivity of negligence. Here, the nature of the action is perhaps less focused on continuous disclosure and more on preventing fraud but section 234 would again limit investor compensation to the wrongdoer’s gain or loss avoidance, of which there may still be none. Section 199 breaches in Singapore have so far been prosecuted through criminal actions.³⁵

PP v. Chen Jiulin provides a good example in the Singapore context of the possible defendants in a securities fraud case, although here involving state criminal, as well as, civil regulatory enforcement. China Aviation Oil Holding Company (“CAOHC”) sold 15% of its stake in its subsidiary CAO (Singapore) to investors through a private placement at the time when it possessed non-public information affecting the subsidiary. CAOHC had undertaken this share placement in order to raise capital to help CAO (Singapore) meet margin calls resulting from over-the-counter oil derivative trading. CAOHC knew of the losses at its subsidiary (which its own independent directors did not), and had to pay a civil penalty of \$8m to the MAS under section 232 for breaching the insider trading provisions of the *Securities and Futures Act (Singapore)*.³⁶ Where continuous disclosure was concerned, none of its realised losses were disclosed to the Singapore Exchange (SGX) as required under section 203(2). Nor were the realised and unrealised losses captured in CAO (Singapore)’s half year and third quarter financial statements, for which the corporation was in breach of section 199(c)(i) of the *Securities and Futures Act (Singapore)*. For consenting to such non-disclosure and misleading statements, its CEO Chen Jiulin pleaded guilty under section 331, read with the two relevant offence creating provisions. He was fined \$330,000 for the section 199 offence and jailed for 3 months for the section 203 offence, but this was because the fact situations overlapped—there were 6 charges altogether, with 9 others taken into consideration. In all, Chen was sentenced to four years and three months’ imprisonment and fined \$335,000. Yet CAO (Singapore) faced neither a civil penalty claim by the MAS, nor criminal prosecution for its misstatements. While too much should not be read into this, it does show that the corporation itself is often not the right defendant in a situation where its shares are closely held by a major shareholder if the rationale for making it pay is deterrence. This will be more fully set out in the next Part.

Consequently, the continuous disclosure provisions in Singapore are in effect enforced through a mix of public sanctions against the issuer company (sections

³⁵ Unlike *Securities and Futures Act (Singapore)*, s. 203, where MAS obtained a penalty of \$75,000 against Trek 2000 International Ltd. in 2006, there has been no civil penalty obtained by MAS for a contravention of *Securities and Futures Act (Singapore)*, s. 199.

³⁶ It has been questioned whether the civil penalty amount was in fact too low: The Lex Column, “China Aviation Oil” *The Financial Times* (20 August 2005).

203 and 199), and the relevant corporate officers (directly through section 199 and indirectly through section 331),³⁷ rather than any form of private civil liability. For the latter, it has been suggested that the proper plaintiff should in principle not be investors but the corporation for whom the individual wrongdoer acts for, for the corporate governance reasons here as well as the difficulty in quantifying losses at the shareholder level discussed below.³⁸

IV. ISSUER AN IMPROPER DEFENDANT

A. Fictional Separate Entity

In the U.K., section 90A of the *Financial Services and Markets Act 2000 (U.K.)* allows purchasers of shares statutory civil claims against issuers for *fraudulent*, though not negligent, periodic misstatements, but *reliance* on the statement must be shown. Thus, it is both like and unlike 10b-5 securities actions in the U.S. It allows buying investors to sue the issuer but an action against directors is expressly excluded by section 90A(6)(b).³⁹ In contrast, while there is no aiding and abetting liability under 10b-5,⁴⁰ direct actions can be brought by shareholders against directors (and controlling persons under section 20(a) of the *Securities Exchange Act 1934 (U.S.)*) although this is much less common than actions against corporate issuers, and individuals seldom actually pay anything in the resulting settlement.⁴¹ In contrast, we have seen that contemporaneous investors in Singapore are often limited to a claim against the issuer (or more exceptionally a director) only for the amount of profit made or loss avoided by the contravening person, and realistically there is usually none in breaches of continuous disclosure. The U.K. Treasury recently accepted the *Final Report* of Paul Davies who had recommended slightly broadening the scope of section 90A by also allowing sellers of securities (as is the case with 10b-5, although neither provision gives holders such standing) to sue the corporation and not just for fraudulent disclosures but also dishonest delays in making disclosure (as opposed to misstatements). It confirmed, however, that directors have a safe harbour from investor action and any action by the issuer against them would still be left to the common law.⁴²

³⁷ See e.g., *Public Prosecutor v. Wong Tai* [2006] SGDC 193; *Tan Hor Peow Victor*, *supra* note 29.

³⁸ See *infra* notes 119-129 and accompanying text.

³⁹ See Wan Wai Yee, "Reconsidering Personal Liability on Directors and Senior Managers for Misstatements and Non-Disclosures to the Securities Market" (2009) 9 J.C.L.S. 235 [*Reconsidering Personal Liability*], criticising *Financial Services and Markets Act 2000 (U.K.)*, s. 90A for expressly excluding investor action against the directors.

⁴⁰ *Stoneridge Investment Partners, LLC v. Scientific Atlanta, Inc.* (2008) 128 S. Ct. 761 [*Stoneridge*]. In August 2009, Senator Arlen Specter introduced a Bill to reverse the effect of *Stoneridge*. Contrast the position in Australia: Angie Zandstra, Jason Harris & Anil Hargovan, "Widening the Net: Accessorial Liability for Continuous Disclosure Contraventions" (2008) 22 Austl. J. Corp. L. 51. See now *ASIC v. Maxwell* (2006) 59 A.C.S.R. 373 (N.S.W.S.C.) at para. 92 [*Maxwell*].

⁴¹ John Coffee Jr., "Reforming the Securities Class Action: An Essay on Deterrence and Its Implementation" (2006) 106 Colum. L. Rev. 1534 at 1550.

⁴² *H.M. Treasury*, *supra* note 4 at para 7.10.

Davies' study was, however, premised on an Anglo-American model of corporation, which may not generally exist in the Singapore context.⁴³ For example, he states that poor disclosure is usually the result of directors trying to do what they believe is in the company's interest, *i.e.*, to keep the company afloat by not disclosing bad news.⁴⁴ There is an assumption of dispersed shareholdings here and with it little structural bias, with the latter having been defined by Claire Hill and Brett McDonnell as a bias against the corporate interest and one in favour of one of the constituencies within the corporation, such as management or controlling shareholders.⁴⁵ But the insider type companies that exist outside the U.S. and U.K. are quite different in that disclosure can be held back or inaccurate for more extrinsic reasons. It remains a fact that U.S.-listed companies have far greater dispersal of shareholdings than Singapore ones, even if it has been argued recently that it is less dispersed than was thought. But the empirical evidence there only shows that in the U.S., 59.74% of U.S. corporations have "controlling shareholders" who hold at least 10% of the shares.⁴⁶ The starting point here is quite different, as most listed companies are held by major shareholders who control about 60 to 70% of the shares.⁴⁷

In Singapore, minority shareholder protection is important as realistically the board will prioritise the interests of the major shareholder.⁴⁸ The more specific point here though is that the shareholder interests are not aligned, and so it becomes more difficult to conceive of the corporation as a separate entity that ought to be liable because of disclosures made on its behalf by its directors. These disclosures do

⁴³ Australian companies are also more insider-based or closely controlled than sometimes thought: Alan Dignam & Michael Galanis, "Australia Inside-Out: The Corporate Governance System of the Australian Listed Market" (2004) 28 *Melb. U.L. Rev.* 623.

⁴⁴ Davies, *Final Report*, *supra* note 4 at para. 2.

⁴⁵ Claire Hill & Brett McDonnell, "Disney, Good Faith, and Structural Bias" (2007) 32 *J. Corp. L.* 833. This was in the context of director liability (to the corporation), where the argument was that structural bias (there favouring management) should make it easier to prove their bad faith. Here the structural bias (directors favouring major shareholders) is also used to argue that the corporation should not be the defendant in disclosure actions as it cannot be seen as a separate entity benefitting from the decisions of the directors. This article argues that, even in cases of disclosure violations, the proper plaintiff is the corporation and the directors should be the defendants.

⁴⁶ Yoser Gadhoom, Larry Lang & Leslie Young, "Who Controls US?" (2005) 11 *Eur. Fin. Mgmt.* 339. See also Leslie Hannah, "The Divorce of Ownership from Control from 1900: Recalibrating Imagined Global Historical Trends" (2007) 49 *Bus. His.* 404 at 423; Joao A.C. Santos & Adrienne S. Rumble, "The American Keiretsu and Universal Banks: Investing, Voting and Sitting on Nonfinancials' Corporate Boards" (2006) 80 *J. Fin. Econ.* 419 at 436; Clifford G. Holderness, "The Myth of Diffuse Ownership in the United States" (2009) 22 *Rev. Fin. Stud.* 1377. These views have been challenged more recently: see Brian Cheffins, "Is Berle and Means Really a Myth?" UCLA School of Law, Law & Economics Research Paper Series, Research Paper No. 09-05 (March 2009), online: <<http://ssrn.com/abstract=1352605>>.

⁴⁷ According to one study, the median proportion of shares owned by blockholders in Singapore is about 63%: see Phillip Phan & Toru Yoshikawa "Corporate Governance in Singapore: Developments and Prognoses", online: <http://www.research.smu.edu.sg/faculty/edge/corp_gov/papers/Singapore%20CG.pdf> at 9. Fox, *Civil Liability and Mandatory Disclosure*, *supra* note 20 at 280 argues that U.S. issuers should be freed from liability even though the predominant legal and economics view is that primary liability is that of the entity: see Reinier H. Kraakman, "Corporate Liability Strategies and the Costs of Legal Controls" (1984) 93 *Yale L.J.* 857 at 858. In disclosure, unlike other management decisions, the corporation is a victim, not beneficiary, unless it issues shares at the same time.

⁴⁸ The different kinds of conflicts within are corporation is the starting point for R. Kraakman *et al.*, *Anatomy of Corporate Law: A Comparative and Functional Approach*, 2nd ed. (New York: Oxford University Press, 2009).

not only have external effects but also affect the different corporate constituencies internally, specifically by affecting their investment decisions in the case of shareholders.⁴⁹ Thus, in Singapore, in a recent case on prospectus disclosure, *Auston International v. Public Prosecutor*⁵⁰ the judge, on appeal, thought that the CEO and CFO were really liable rather than the company, even though at common law it has been held that a company remains liable even where a prospectus had been prepared by professionals.⁵¹ For such disclosure both the issuer and directors are clearly statutorily liable under sections 253 (criminal) and 254 (civil) of the *Securities and Futures Act (Singapore)* as the prospectus speaks directly to the incoming shareholders, which may not be the case with continuing disclosure, but Lee Seiu Kin J. severely reduced the fine that had been imposed on the issuer on the basis that a deterrent sentence had no effect on the corporation, as opposed to the individuals managing it.⁵² While the investor protection rationale is more important than corporate governance and structural bias concerns where prospectus disclosure is involved, the case recognises that in closed companies the separate entity is not a monolithic whole, and liability should attach to a more culpable constituency within it.⁵³

There are further structural problems created if the remedy for disclosure violations is targeted at the fictional separate entity. In *ASIC v. Chemeq*,⁵⁴ French J. said:

It may also be relevant to consider the impact, if any, on shareholders when a penalty is sought against a corporation. Penalties imposed on officers of the corporation for their part in such contraventions affect those officers alone. Penalties imposed on the corporation may affect shareholders including those who have become shareholders on a set of assumptions induced by the very non-disclosure complained of. In some cases it is possible also that creditors may be affected. Who then is being deterred when only the corporation is penalised? I am not sure that there is a satisfactory answer to this concern within the present statutory scheme. One might imagine that if a penalty is to be significant to a corporation

⁴⁹ Poorer disclosure could lead to less liquidity which reduces the value of shares: Fox, *Civil Liability and Mandatory Disclosure*, *supra* note 20 at 280.

⁵⁰ *Auston International v. Public Prosecutor* [2007] SGHC 219 [*Auston International*].

⁵¹ Eillis Ferran, *Principles of Corporate Finance Law* (New York: Oxford University Press, 2008) at 446 [*Principles of Corporate Finance Law*], citing *Lynde v. Anglo-Italian Hemp Co.* [1896] 1 Ch. 178, *Mair v. Rio Grande Rubber Estates* [1913] A.C. 853.

⁵² *Auston International*, *supra* note 50 at para. 19. In fact, for prospectus liability under the U.S. *Securities Act 1933*, s. 11, the company is strictly liable, while officers, directors and third party intermediaries are only liable for negligence as they are provided with a due diligence defence. The quasi-due diligence defence in *Securities and Futures Act (Singapore)*, s. 255 is less clear as to who can rely on it, but it is unlikely that the issuer corporation itself can do so.

⁵³ But there is arguably structural bias even in the case of corporate disclosure where the Anglo-American conception of the company is concerned because when directors choose to make disclosure or not at all may favour a particular generation of shareholders: Henry T.C. Hu, "New Financial Products, the Modern Process of Financial Innovation, and the Puzzle of Shareholder Welfare" (1991) 68 *Texas L. Rev.* 1273 at 1300. See further Hans Tjio, "Rationalisation of Directors' Duties" 17 (2005) *S.Ac.L.J.* 52 [*Rationalisation of Directors' Duties*] where it was argued that directors should consequently owe a duty to act fairly to future shareholders. But the latter's interests are best protected where the corporation is the plaintiff as they are unable to enforce their sometimes putative rights, particularly if reliance has to be shown.

⁵⁴ [2006] F.C.A. 936, (2006) 58 A.C.S.R. 169 at para. 98.

it will also be significant to its shareholders in its impact on the capital which backs their shares. In a company with capitalisation as high as that of Chemeq, the impact on individual shareholders may be insignificant. The penalties that count most are likely to be those imposed on the responsible individuals. Nevertheless the law as presently framed requires the assumption that the contravening corporation is a person distinct from its shareholders and that it can be deterred by the imposition of appropriate penalties.

More recently, in the U.S., Rakoff J. in the Southern District of New York rejected the settlement under which the Bank of America would pay the SEC a fine of US\$33 million for disclosure violations in its merger with Merrill Lynch (concerning bonuses payable to the latter's executives), stating that "[t]his proposal to have the victim of the violation pay an additional penalty for their own victimisation was enough to give this court pause."⁵⁵

If the remedy for disclosure violations is not properly tailored, a group or generation of shareholders may end up losing twice over, particularly if they are unable to be part of the plaintiff group (for reasons such as a failure to prove reliance, which is a hurdle in most jurisdictions other than the U.S., discussed in the next Part). This issue will be discussed further when we examine why investors should not be the plaintiffs in most securities disclosure litigation and is something that Davies acknowledged in his *Final Report*. However, he thought that issuer liability under section 90A of the *Financial Services and Markets Act 2000 (U.K.)* ought to remain because "fraud is so corrosive of the basic trust on which the market operates that civil liability for such statements performs a valuable public function in deterring fraud."⁵⁶ It has also been said that existing shareholders that hold on to the shares instead of trading actively should still ultimately bear the loss that arises when the company pays as they have a role and responsibility in monitoring fraud, and their indirect liability gives them an incentive to do this properly.⁵⁷ However, the countervailing argument is that the shareholders have little power at the moment, particularly in the U.S., to remove directors, and in any case the board itself may not control management.⁵⁸ Also, the focus on shareholders is usually on their rights, and here we are imposing an obligation on them to monitor, with all the attendant collective action problems. Further, in insider type companies, the major shareholder will be the one in control of the board, and so there is little reason to make minorities responsible for a share of the compensation paid by the corporation for the misleading disclosures that are made by or with the knowledge of the major shareholder. Indeed, it may be that major shareholders that are privy to disclosure violations should be formally recognised as

⁵⁵ *SEC v. Bank of America Corporation* (2009) Civ 6829 (S.D.N.Y.). The actions discussed here were all regulatory in nature and in this context the SEC conceded that they would usually "go after the company executives who were responsible", but it did not do so here as the evidence clearly showed that the misleading disclosures were drafted by lawyers on behalf of the bank.

⁵⁶ Davies, *Final Report*, *supra* note 4 at para. 22.

⁵⁷ Lawrence E. Mitchell, "The 'Innocent Shareholder': An Essay on Compensation and Deterrence in Securities Class-Action Lawsuits" [2009] Wis. L. Rev. 243 at 295.

⁵⁸ Jill E. Fisch, "Confronting the Circularity Problem in Private Securities Litigation" (2009) Wis. L. Rev. 333 at 340-341 [*Confronting the Circularity Problem*]. It is not clear that shareholders should be given more powers to remove boards: Lynn A. Stout, "The Mythical Benefits of Shareholder Control" (2006) 93 Va. L. Rev. 789.

possible direct defendants such as is the case under section 20(a) of the *Securities Exchange Act 1934 (U.S.)* which imposes liability (joint and several) on controlling persons, “unless the controlling person acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action.” We have seen, however, that even directors and officers are not usually liable there under their 10b-5 actions (issuers are), and in any case in an outsider system, it would be highly unusual for a shareholder to have any significant degree of involvement in the disclosure mechanisms of a listed company. That, though, is not the case in Singapore and much can be said for imposing direct liability on controlling shareholders involved in disclosure violations even where they do not trade whilst in possession of inside information.

In any case, incentives for existing shareholders to improve corporate governance also exist where the corporation is the plaintiff, and the mechanism for them to achieve this is the statutory derivative action, and where the costs are borne by the company.⁵⁹ This is discussed later at Part V.B.

B. Existing Difficulties of Class Actions against Issuer: *Reliance and Causation*

It appears that the U.K. has not gone about the implementation of the *Transparency Directive (E.U.)* in the specific instance of section 90A of the *Financial Services and Markets Act 2000 (U.K.)* with great enthusiasm. We have seen that Davies stressed that public enforcement is still the main avenue to prosecute breaches of continuous disclosure. He also expressed some scepticism regarding private enforcement, and its remedial consequences, but was assuaged by the fact that liability is based on a *fraud* threshold, which will be examined in the next Part. But, perhaps most importantly, section 90A is difficult for large groups of shareholders to actually use, in that there is the need to show reasonable *reliance*,⁶⁰ *i.e.*, that the claimants were induced to act by the deceit or misrepresentation by the issuer. This is the common law position which does not trouble the present prospectus disclosure regime,⁶¹ and which many U.S. 10b-5 actions overcome with the fraud on the market theory from *Basic, Inc. v. Levinson*⁶² where the Supreme Court thought that there was a

⁵⁹ Hans Tjio & Wee Meng Seng, “Foss v Harbottle in the Singapore Court of Appeal” (2008) C. & S.L.J. 333 at 343 [Tjio & Wee].

⁶⁰ See *Financial Services and Markets Act 2000 (U.K.)*, s. 90A(5). The need for reliance in the context of common law claims for negligence and misrepresentation has been reaffirmed in *J.P. Morgan Chase Bank v. Springwell Navigation Corporation* [2008] EWHC 1186.

⁶¹ Ferran, *Principles of Corporate Finance Law*, *supra* note 51 at 456; Loke, *Efficacy of Securities Investors’ Rights in Singapore*, *supra* note 33 at 119 to 124.

⁶² 485 U.S. 224 (1988) at 247. See now Donald C. Langevoort, “Basic at Twenty: Rethinking Fraud on the Market” (2009) Wis. L. Rev. 151 [Rethinking Fraud on the Market]. He points out that while reliance was supposed to become less of an issue with the presumption, the difficult hurdles for litigants to cross were intended to be materiality and the measurement of damages (at 165). Where the latter is concerned, this seems to be the case after *Dura Pharmaceuticals, Inc. v. Broudo* (2005) 544 U.S. 336 [Dura Pharma], see *infra* note 71 *et seq.* and accompanying text. For materiality, see Yvonne C.L. Lee, “The Elusive Concept of Materiality under U.S. Federal Securities Laws” (2004) 40 Willamette L. Rev. 661 who has examined the materiality provisions in the European Union, Australia and Hong Kong and highlighted the difference with the U.S. approach in their focus on the effect of the relevant corporate information on

“rebuttable presumption of reliance” where “materially misleading statements have been disseminated into an impersonal, well-developed market for securities.” This imputes a reliance on the integrity of the market price and takes the focus away from the actual investment decisions of each claimant.

Consequently, class actions are difficult to organise under section 90A, even if they were procedurally available, which formally they are not. But it will be seen below that such actions may serve little deterrence or compensatory function in any event. This also appears to be the position in Singapore where neither sections 199 nor 203 of the *Securities and Futures Act (Singapore)* create any presumption of reliance. It is less clear in Australia where specific representative proceedings were introduced in 1992 into Part IVA of the *Federal Court of Australia Act 1976 (Cth)* and there have been investor class actions.⁶³ In the context of disclosure violations, section 1041E of the *Corporations Act 2001 (Cth)* (similar to section 199 of the *Securities and Futures Act (Singapore)*) read with section 1041I (which allows a person who suffers loss or damage because of conduct “in relation to a financial product or a financial service” that is misleading or deceptive to recover against the wrongdoer) clearly allows investors a cause of action against the statement maker for losses caused by the misstatement, and the question of reliance and its presumption has been discussed in the courts⁶⁴ the Corporations and Markets Advisory Committee⁶⁵ and by academics.⁶⁶ But, even in the U.S., securities class actions have been under attack since at least *Basic*.⁶⁷ And, in cases where corporate statements are not made to an efficient market, where fraud on the market cannot be utilised, the U.S. Supreme Court has recently required a strong form of reliance in *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.*,⁶⁸ and stated that the use of common law analogies could in fact wrongly expand the

the price of securities (rather than on the investment decisions of the reasonable investor). Langevoort is “not averse to the idea of addressing materiality as a matter of law,” and not fact: Langevoort, *Rethinking Fraud on the Market*, *ibid.* at 196.

⁶³ Boros, *Public and Private Enforcement*, *supra* note 13. See also “Introduction” in K.E. Lindgren ed., *Investor Class Actions* (Sydney: Ross Parsons Centre, University of Sydney, 2009) at vii.

⁶⁴ In *Dorajay Pty. Ltd. v. Aristocrat Leisure Ltd.* [2008] F.C.A. 1311, which was settled, the shareholders had signed a statutory declaration of reliance but it was also argued that each shareholder did not have to show reliance on the alleged misconduct: Vince Morahito, “Revisiting Australia’s first shareholder class action” in Lindgren, *ibid.* at 58 and 110. But see now *Ingot Capital Investments Pty. Ltd. & Ors v. Macquarie Equity Capital Markets Ltd. & Ors* [2008] NSWCA 206 where reliance was required for an action for their statutory claims for misleading and deceptive conduct under the *Corporations Act 2001 (Cth.)*, as is the case under the *Trade Practices Act (Cth.)*. For the requirement at common law, see *supra* note 60.

⁶⁵ The Corporations and Markets Advisory Committee, while discussing it, did not issue any recommendations: see Sweet & Maxwell’s Company Law Newsletter, Issue 238 (2 October 2008).

⁶⁶ Mark Humphrey von Jenner, “Causation in Fraud on the Market Actions in Australia” (6 November 2008), online: <<http://ssrn.com/abstract=1296310>>, argues (at 12) that it is likely that legislature intended the presumption to apply to market manipulation. Compare Peter Cashman, “Prospects and problems for investors in class action proceedings” in Lindgren, *supra* note 63 at 78-83.

⁶⁷ Barbara Black, “Eliminating Securities Fraud Class Actions Under the Radar” (6 April 2009), University of Cincinnati Public Law Research Paper No. 09-08, online: <<http://ssrn.com/abstract=1373878>>.

⁶⁸ *Supra* note 40, noted in Franklin A. Gevurtz, “Law Upside Down: A Critical Essay on *Stoneridge Investment Partners, LLC v. Scientific Atlanta, Inc.*” (2009) 103 *Northwest. U. L. Rev.* 448. The defendants in *Stoneridge* were counterparties that placed advertisements with the issuer to boost the latter’s advertising revenue. In return, the issuer overpaid for cable boxes that the defendants sold, and documents were backdated to cover up the fact that no net revenue was generated by the arrangement.

scope of 10b-5 liability.⁶⁹ In contrast, the earlier decision in *Basic* had warned that the common law should not be used to unduly restrict the scope of the statutory claim.⁷⁰

In any case, we will see that the presumption of reliance may not help much as *Dura Pharmaceuticals, Inc. v. Broudo*⁷¹ requires the proof of actual decline in share prices due to the inaccurate disclosures, as opposed to overvaluation at the time of purchase, in order to sue for securities fraud. The Supreme Court stated that “as a matter of pure logic, at the moment the transaction takes place, the plaintiff has suffered no loss; the inflated purchase payment is offset by ownership of a share that at that instant possesses equivalent value.”⁷² Although the reasoning is different, the requirement that the seller may in practice have to sell to crystallise a loss sounds quite similar to the rule in *Houldsworth v. City of Glasgow Bank*,⁷³ which requires shareholders to rescind a share purchase before they can claim damages from the company. While that position has been reversed by statute in the U.K. by section 111A of the *Companies Act 1985 (U.K.)*, which was inserted by the *Companies Act 1989 (U.K.)* (now section 655 of the *Companies Act 2006 (U.K.)*), it is a rule which may still be applicable in Singapore, given that no such similar provision has been introduced into the *Companies Act (Singapore)*⁷⁴ here. In Australia, it has been held that the rule does not apply to both purchasers on the open market, and even perhaps subscribers for shares, who have statutory claims for deceptive and misleading conduct against a company that has breached its continuous disclosure obligations.⁷⁵ Although the rationale for the rule in *Houldsworth* was capital maintenance, it could in the modern day context be seen as a difficulty with conceptualising a loss when a subscriber still holds onto the shares.

Reliance is thus only one part of causation, *i.e.*, purchase causation, and loss causation still has to be shown. Not separating the two can make it either too easy, or too difficult, to prove a loss. It has been argued that Australian courts have not

⁶⁹ *Stoneridge, ibid.* at 771.

⁷⁰ See Jill E. Fisch, “Cause for Concern, Causation and Federal Securities Fraud” (2009) 94 Iowa L. Rev. 811 at 829 [*Cause for Concern*]. She also points out (at 813) that in the interim, in *Dura Pharma, supra* note 62 at 343, the Supreme Court had said that the causation rules in the 10b-5 action were based on common law deceit and misrepresentation. Compare further *Blue Chip Stamps v. Manor Drug Stores* (1975) 421 U.S. 723 at 744-745 [*Blue Chips*], that “(t)he typical fact situation in which the classic tort of misrepresentation and deceit evolved was light years away from the world of commercial transactions to which Rule 10b-5 is applicable.”

⁷¹ (2005) 544 U.S. 336.

⁷² *Ibid.* at 342. See also Fisch, *Cause for Concern, supra* note 70 at 845, as to why share ownership may be different from other forms of property ownership, and she consequently questions why a price drop without a sale seems to be enough in the former (at 847).

⁷³ (1880) 5 App. Cas. 317.

⁷⁴ Cap. 50, 2006 Rev. Ed. Sing. [*Companies Act (Singapore)*].

⁷⁵ *Sons of Gwalia Ltd. v. Margaretic* [2007] H.C.A. 1. The claimants would be treated as creditors of the company and would rank equally with unsecured creditors for the amounts of their claims but this is seen as fatal to the Australian insolvency regime: see Andrew Bilski & Patrick Brown “Sons of Gwalia versus shareholder subordination: Fairness versus Efficiency” (2008) 26 C. & S.L.J. 93. See also *Cadence Asset Management Pty. Ltd. v. Concept Stores Ltd.* [2005] F.C.A.F.C. 265. See further Elizabeth Boros, “Shareholder litigation after *Sons of Gwalia v Margaretic*” (2008) 26 C. & S.L.J. 235 [*Shareholder Litigation after Sons of Gwalia v Margaretic*]. The U.K. Treasury has stated that it will monitor how the Australian Corporations and Markets Advisory Committee deals with *Gwalia: supra* note 4 at para. 7.14, accepting Davies’ view that it has implications for other areas such as capital maintenance.

distinguished the two in the context of section 1041I, and this has been manifested in the “confused” approach there.⁷⁶ One U.S. Fifth Circuit case, however, required the establishment of loss causation before the presumption of reliance could be used to certify class actions,⁷⁷ which Jill Fisch thought may have been accepted by the Supreme Court in *Stoneridge* where Kennedy J. said that “reliance is tied to causation, leading to the inquiry whether respondent’s acts were immediate or remote to the injury.”⁷⁸ While this is unlikely to have been the case, it shows the continuing concern with investor actions against issuers that may have begun to be addressed in 1995 where the *Private Securities Litigation Reform Act (U.S.)* introduced section 21(D)(b)(4) to the *Securities Exchange Act 1934 (U.S.)*. This states that “the plaintiff shall have the burden of proof that the act or omission of the defendant alleged to violate this chapter caused the loss for which the plaintiff seeks to recover damages.”⁷⁹ Fisch has pointed, however, that “from *Basic* to *Dura*, the Supreme Court has refused to address the issue of what constitutes an appropriate economic loss”⁸⁰ in the case of shareholder suits. Davies has also said that he did not think that the causation rules for section 90A of the *Financial Services and Markets Act 2000 (U.K.)* should be codified and thought it was premature to assume the fraud measure of directness which was something he had appeared to do initially.⁸¹ The U.K. Treasury accepted his recommendation in the *Final Report* to leave it to the courts but that this would likely mean that “damages are likely to be assessed by reference to the loss caused by reliance on the statement, and not the loss caused by its falsity.”⁸² This, though, is closer to the fraud measure than what seems to be the position in the U.S.

Dura Pharma held that even where there has been a sale, which crystallises the loss, the lower share price at the point of sale could be caused by many different intervening factors and not the relevant information. The U.S. Supreme Court said that:

The lower price after corrective disclosure may reflect, not the earlier misrepresentation, but changed economic circumstances, changed investor expectations, new industry-specific or firm-specific facts, conditions or other events, which taken separately or together account for some or all of the reduced price

⁷⁶ *von Jenner*, *supra* note 66 at 9, and now Ashley Black, “Commentary on all four papers” in Lindgren, *supra* note 63 at 107. See also Langevoort, *Rethinking Fraud on the Market*, *supra* note 62 at 180, suggesting that the two issues have often been conflated in the U.S.

⁷⁷ *Oscar Private Equity Investments v. Allegiance Telecom, Inc.* (2007) 487 F. 3d. 261. See Langevoort, *Rethinking Fraud on the Market*, *supra* note 62 at 185-186. Certification is required in the U.S., where it must, amongst other things, be shown that the common issues predominate. In securities class actions, this can be satisfied if the market was efficient so that the fraud on the market theory applies. There is no formal requirement for certification in Australia: Geoffrey Miller, “Some thoughts on Australian class actions in the light of the American experience” in Lindgren, *supra* note 63 at 5-6.

⁷⁸ *Stoneridge*, *supra* note 40 at 770, and see Fisch, *Cause for Concern*, *supra* note 70 at 829.

⁷⁹ 15 U.S.C. §78u-4(b)(4) (2000).

⁸⁰ Fisch, *Cause for Concern*, *supra* note 70 in the abstract.

⁸¹ Paul Davies Q.C., *Davies Review of Issuer Liability, Liability for Misstatements to the Market* (March 2007), online: <http://www.hm-treasury.gov.uk/d/davies_discussionpaper_260307.pdf> at para. 107 [*Review of Issuer Liability*]. At para. 109, he contrasted the causation rules in 10b-5, which he thought was closer to the negligence measure, despite its “fraud basis”.

⁸² *H.M. Treasury*, *supra* note 4 at para. 7.12, quoting Davies, *Final Report*, *supra* note 4 at para. 60.

The longer the time period between purchase and sale, the more likely that other factors caused the loss.⁸³

In its pleadings, a plaintiff is expected to provide the defendants “notice of what the relevant economic loss might be or of what the causal connection might be between that loss and the misrepresentation.”⁸⁴ The experience of English courts with claims for falls in property prices due to negligent valuations is that it is difficult to measure loss where there is a general market fall. In *South Australia Asset Management Corp v. York Montague Ltd.*,⁸⁵ Lord Hoffmann required the plaintiff to “show that the duty was owed to him and that it was a duty in respect of the kind of loss which he has suffered.” The language of legal responsibility (or scope of the duty that is broken) has been used particularly in cases of negligence to prevent full recovery of economic losses. But Fisch has pointed out that for common law fraud in the U.S., “courts rarely consider proximate cause extensively.”⁸⁶ Yet, she grants this is done in cases of securities fraud litigation due to the fact that courts are not sure of the value of the relevant information and its impact on stock prices.⁸⁷ In the context of negligence, proximate cause was recently discussed by the Singapore Court of Appeal in *JSI Shipping (S) Pte. Ltd. v. Teofoongwonglcong (a firm)*.⁸⁸

By way of introduction, we must clarify that the “but for” test is a necessary but sometimes insufficient litmus test. It is but an exclusionary test serving to filter out non-causal occasions for the loss (John G Fleming, *The Law of Torts* (The Law Book Company Limited, 9th Ed, 1998) at p 220; Harvey McGregor, *McGregor on Damages* (Sweet & Maxwell, 17th Ed, 2003) at para 6-008). Therefore, the respondent’s failure to verify Riggs’ remuneration may survive this test, but may still not qualify as an “effective cause” or “proximate cause”, a concept used to determine whether it is fair to hold the negligence responsible for the loss where other factors have contributed to or intervened in the chain of causation (AM Dugdale & KM Stanton, *Professional Negligence* (Butterworths, 3rd Ed, 1998) at para 18.01; *Chitty on Contracts* vol 1 (Sweet & Maxwell, 29th Ed, 2004) at para 26-029). The elusiveness of such a concept was incisively alluded to by Andrews J in *Helen Palsgraf v The Long Island Railroad Company* (1928) 248 NY 339 at 352, where he opined that “proximate” means that “because of convenience, of public policy, of a rough sense of justice, the law arbitrarily declines to trace a series of events beyond a certain point. This is not logic. It is practical politics”.

The policy objectives behind such an approach to loss causation was perhaps most clearly seen in the judgment of Mummery L.J. in *Swindle v. Harrison*,⁸⁹ another property fall case in the U.K. but involving a breach of fiduciary duties by solicitors, where (without citing the case) he applied the approach in *South Australia*. In

⁸³ *Dura Pharma*, *supra* note 62 at 343.

⁸⁴ *Ibid.* at 346.

⁸⁵ [1997] A.C. 191 (H.L.) at 211.

⁸⁶ Fisch, *Cause for Concern*, *supra* note 70 at 832. See also Davies, *Review of Issuer Liability*, *supra* note 81 at para. 109.

⁸⁷ Fisch, *Cause for Concern*, *supra* note 70 at 845-846.

⁸⁸ [2007] 4 S.L.R. 460 at para. 141.

⁸⁹ [1997] 4 All E.R. 705 (C.A.) [*Swindle*], noted in Hans Tjio & Yeo Tiong Min, “Limited Liability for Breach of Fiduciary Duty” (1998) 114 L.Q.R. 181.

contrast, Evans L.J., who expressly applied *South Australia*, only did so because it was a not a *fraudulent* breach of fiduciary duty. Mummery L.J.'s approach focusing on the kinds of risk at stake could justify a more stringent loss causation requirement for securities fraud, even if remoteness of damage is treated separately and is based on the rule of directness (and without the need for foreseeability) in *Doyle v. Olby (Ironmongers) Ltd.*⁹⁰

We have a slightly different set of problems with loss measurement in Singapore. Section 234 of the *Securities and Futures Act (Singapore)* expressly provides that loss is calculated by measuring the difference between the price at which the securities were dealt with in that transaction and their "likely" price if the contravention had not been committed.⁹¹ While this formulation does not work for insider trading,⁹² it does provide a clear method of determining loss in cases where there has been a breach of the continuous disclosure requirements in section 203 or the proscription against misleading statements in section 199. But it is not clear that it does away with the need to prove causation or that intervening factors could sever the link between the inflated purchase price and the "likely" price had the disclosures been made promptly and accurately. A more fundamental problem we have seen is that the maximum recoverable amount is linked to profit gained or loss avoided by the contravening persons.

With section 90A of the *Financial Services and Markets Act 2000 (U.K.)*, as is the case in Singapore under section 234, therefore, investor actions against issuers are severely hampered by the lack of a fraud on the market theory, which militates against any actions by most investors due to the costs of securities litigation and collective action problems. Under the statutory provisions in Singapore, it may also be difficult to ascertain investor loss, which is something that has recently troubled the U.S. courts. Further, it relates that loss to the wrongdoer's gain, which makes sense in the case of insider trading (where, conversely, the calculation of the loss may not be meaningful), but less so in cases of poor corporate disclosure. In contrast, we will see that actions taken by a company against its directors for false and misleading disclosures may be treated as analogous to traditional common law or equitable fraud, where causation requirements are quite relaxed, and it is likely that losses do

⁹⁰ [1969] 2 Q.B. 158 (C.A.) [*Doyle*]. von Jenner, *supra* note 66 at 12 treats loss causation differently from remoteness and argues for qualitative causation in the former (alongside presumed reliance for purchase causation) but a directness test for the latter. Fisch, *Cause for Concern*, *supra* note 70 at 830-832 does not in her discussion of "proximate cause" distinguish the two, and it may be that many courts similarly do not differentiate them. At 831, Fisch points out that phrase "proximate cause" has been replaced by the concept of legal responsibility in the *Restatement (Third) of Torts*, §29.

⁹¹ This measure was used for the provisions on market misconduct other than insider trading in *Securities Industry Act 1983 (Malaysia)*, s. 88A. The new *Capital Markets and Services Act 2007 (Malaysia)*, s. 199 does not define "loss or damage". It differs from the measure used there for most forms of insider trading, where s. 201(3) and (4) provide that a claimant's loss is measured by the difference in the price at which the products were applied for, or agreed to be applied for, by the insider or the other person and the price at which they would have been likely to have been disposed of in a disposal made at the time of the application or the time of the agreement, as the case may be, if the information had been generally available. The latter method of calculating loss in insider trading cases is similar to that in Australia's *Corporations Act 2001 (Cth.)*, s. 1043L(2).

⁹² It is difficult to take a purposive interpretation and hypothesise that the likely price should be that in which the seller had sold without contravening the law by making full disclosure, as the means to disclose corporate information are usually not in the seller's hands in cases of insider trading.

not have to even flow from the falsity of the misrepresentation.⁹³ It may therefore be preferable to have the loss proved at the corporate level rather than at the shareholder level. But this requires a fraud standard of liability.

C. Fraud as the Standard of Liability

In his *Final Report*, Davies said that “the tort of deceit is a form of wrongdoing developed by the common law specifically to deal with misstatements,”⁹⁴ in contrast with the tort of negligence which applies generally to different factual matrices. While there may have been a time when gross negligence was seen as “misfeasance or breach of trust,”⁹⁵ it has been pointed out that the gap between the two was never properly explained,⁹⁶ especially as liability for gross negligence depended on the establishment of a duty of care (as with negligence *simpliciter*). Thus, Davies in his *Final Report* cites Millett J. in *Armitage v. Nurse*⁹⁷ for the point his Lordship made about the common law’s inability to distinguish between negligence and gross negligence.

It is clear that the concern with negligence liability is that it is over-encompassing and may lead to defensive reporting,⁹⁸ where less useful information is provided by issuers than would otherwise have been the case. It has also been pointed out that “[f]irms subject to the Federal securities law may, in some situations, rationally choose to obscure or delay negative information in order to maximize welfare of shareholders at the time of the fraud,”⁹⁹ which partly explains the *scienter* requirement in 10b-5 actions. It is difficult to fault the corporation where it is balancing the interests of different constituencies within it, which is why it should not be the defendant in securities disclosure cases. Even where it can be a defendant as in the case of section 90A of the *Financial Services and Markets Act 2000 (U.K.)*, there is presently no liability for delayed disclosures, and the U.K. Government has accepted Davies’ recommendation to require dishonesty before delayed disclosures are actionable.¹⁰⁰ In contrast, the civil liability provision in section 203 of the *Securities and Futures Act (Singapore)* catches negligent issuers that fail to notify its securities exchange of such information as is required under its listing rules or other requirements. And, in Australia continuous disclosure liability is strict but subject to a due diligence defence for parties other than the issuer entity.¹⁰¹ Fox’s proposed civil liability system is also that directors, officers and third party certifiers such as investment banks should have liability attached to them in periodic disclosure in a way similar to the

⁹³ See Davies, *Review of Issuer Liability*, *supra* note 81 at para. 107, and *infra* note 139 *et seq.* and accompanying text.

⁹⁴ Davies, *Final Report*, *supra* note 4 at para. 8. But see further *supra* note 70.

⁹⁵ *Re County Marine Insurance, Rance’s Case* (1870) L.R. 6 Ch. App. 104 at 110 *per* Lord Romilly M.R.

⁹⁶ See William M. Heath, “The director’s ‘fiduciary’ duty of care and skill: A misnomer” (2007) 25 C. & S.L.J. 370 at 387-389.

⁹⁷ [1998] Ch. 241, and Davies, *Final Report*, *supra* note 4 at para. 25.

⁹⁸ Davies, *Final Report*, *supra* note 4 at para. 23.

⁹⁹ James C. Spindler, “Why Shareholders Want Their CEOs to Lie More after Dura Pharmaceuticals” (2007) 95 Georgetown L.J. 653 at 656-657.

¹⁰⁰ *Supra* note 4 at Ch. 6.

¹⁰¹ *Corporations Act 2001 (Cth)*, s. 674. See also Boros, *Public and Private Enforcement*, *supra* note 13.

liability they bear in public offerings, *i.e.*, strict liability subject to a due diligence defence.¹⁰²

In contrast, both section 90A of the *Financial Services and Markets Act 2000 (U.K.)* and section 199 of the *Securities and Futures Act (Singapore)* rely largely on the *Derry v. Peek*¹⁰³ requirement for fraud. It is true that the House of Lords' subjective test in that case led to the *Directors Liability Act 1890 (U.K.)* which created strict liability for prospectus disclosure. However, its application today in the secondary markets for continuous disclosure should be welcomed by those uncomfortable with the negligence liability imposed on issuers by section 203 of the *Securities and Futures Act (Singapore)*, and yet fearful of the difficulties in proving fraud under section 199. It was held in *Public Prosecutor v. Wang Ziyi Able*¹⁰⁴ that given the construction of section 199, which imposes an obligation on a person not to make false and misleading statements, the section 199(i) limb required some form of recklessness of the type in *Derry v. Peek* in spite of its seemingly objective wording, *viz.*, "he does not care whether the statement is true or false." However, Rajah J.A. (sitting in the High Court hearing an appeal from the District Court) stated that "objective analysis can only constitute evidence, albeit often relatively *strong* evidence, for the purposes of the s 199(i) *mens reas.*"¹⁰⁵ While this was in the context of misstatements put up by a private individual on an online financial portal, Davies also says of the fraud standard in section 90A of the *Financial Services and Markets Act 2000 (U.K.)*, that "(t)he risk of being disbelieved also means that, at the margin, fraud liability generates some incentive to check the facts before speaking."¹⁰⁶

The imposition of evidential burdens against the statement maker helps where the corporation is the defendant. Without it, it is not obvious how fraudulent liability is to be attributable to the corporation for periodic financial statements, since that is a statement put out by the corporation where the input of many individuals are aggregated.¹⁰⁷ There would be a need to identify the relevant person whose fraudulent intent could be attributed to the company.¹⁰⁸ The new corporate derivative liability provisions in Division 5 Subdivision 1 of the *Securities and Futures Act (Singapore)* requires that an *offence* has been created by an individual where there is proof of "consent or connivance" or a *contravention* (leading to a civil penalty or claim only) that is "attributable to the negligence" on the part of a corporation.¹⁰⁹ There may be difficulties in this as the language is taken from section 331 of the *Securities and*

¹⁰² Fox, *Civil Liability and Mandatory Disclosure*, *supra* note 20 at 284.

¹⁰³ (1889) 14 App. Cas. 377.

¹⁰⁴ [2007] SGHC 204 [*Wang Ziyi Able*], discussed by Toh, *supra* note 29.

¹⁰⁵ *Ibid.*, at para. 88. In contrast, the alternative *mens rea* in *Securities and Futures Act (Singapore)*, s. 199(ii), which is that "he knows or ought reasonably to have known that the statement or information is false or misleading in a *material particular*", includes negligence as to the accuracy of the information. See also *Wu Yang Construction Ltd. v. Zhejiang Jinyi* [2006] 4 S.L.R. 451 (H.C.). Compare *Vallance v. The Queen* (1961) 108 CLR 56, 83 that "[t]he state of mind of a person, though subjective, is proved by objective evidence."

¹⁰⁶ Davies, *Final Report*, *supra* note 4 at para. 28.

¹⁰⁷ Gevurtz, *supra* note 68 at 452.

¹⁰⁸ *Financial Services and Markets Act 2000 (U.K.)*, s. 90A(4) attributes the knowledge of a person discharging managerial responsibilities within an issuer to the company. This includes directors and senior executives who are responsible for publication of relevant information: s. 90A(9).

¹⁰⁹ *Securities and Futures Act (Singapore)*, ss. 236A to D, introduced by the *Securities and Futures (Amendment) Act 2009*.

Futures Act (Singapore), but that applies in the reverse scenario, *i.e.*, of an officer of the body corporate being liable because the body corporate has contravened a provision in the Act. With these new provisions, we still have to identify a second officer within the corporation, perhaps on some kind of agency or “directing mind and will” basis,¹¹⁰ that consented, connived in or was negligent in the first officer’s wrongdoing. In contrast, the evidential approach allows adverse inferences to be drawn against a corporation where its officers fail to explain how a periodic financial statement was put out inaccurately given the structural procedures or safeguards they had or had not installed in the corporation.

At the same time, directors, particularly in closely held companies, will clearly find it difficult to argue that they were not reckless about the outcome of their failure to comply with disclosure requirements, and so a negligence standard is not required in Singapore. In September 2006, SGX amended rule 705 of its listing rules to require directors of a listed company to “provide a confirmation that, to the best of their knowledge, nothing has come to the attention of the board of directors which may render the interim financial results to be false or misleading.” This attributes a statement directly to a director, and is a potential source of liability under section 199 of the *Securities and Futures Act (Singapore)*.¹¹¹ This would be the case particularly where there is a structural bias that would tilt any decision of the directors in favour of one of the corporate constituencies, such as the major shareholder. In such instances, Hill and McDonnell, in their analysis of the good faith standard (which is distinct from due care and loyalty-conflict duties) for directors in the U.S. (which in the *Disney* case was set at a “conscious disregard of one’s responsibilities,”¹¹² and is close to the recklessness standard discussed here) have argued that bad faith can be proved by both showing structural bias and gross negligence.¹¹³ Similarly, it would be difficult for a director to shift the evidential burden imposed on him where objective facts suggested that he was reckless in not making the necessary inquiries against a background showing structural bias favouring a major shareholder. The concept here is not dissimilar to “fraud on a power”,¹¹⁴ where it is the office and its nature that determines the extent of the duty imposed on the director, and not the power itself. “No power is fiduciary *per se*”;¹¹⁵ and it is the fact that it is vested in an office holder that it becomes a fiduciary power, which then sets boundaries on

¹¹⁰ In cases of fraud, it appears that only the state of mind of the company’s directing mind and will is attributed to it: *In re Hampshire Land Company* [1896] 2 Ch. 743, and not that of an officer that is otherwise attributed to the company in non-fraud situations. See now *Moore Stephens v. Stone Rolls Ltd. (in liquidation)* [2009] UKHL 39 [Moore Stephens].

¹¹¹ The Singapore Exchange (SGX) argued during the trial of Airocean directors who were facing charges of consenting to Airocean’s “reckless failure” to notify the SGX of relevant information concerning its CEO’s questioning by the CPIB that a duty of disclosure falls on all board members, including independent directors: Jamie Lee, “Airocean trial opens with listing rules debate” *Business Times* (12 August 2009).

¹¹² *In re Walt Disney Co. Derivative Litigation*, 906 A. 2d 27 at 62 (Del. S.C. 2006). The Supreme Court upheld the decisions of the Chancery Court to dismiss all claims based on loyalty, care and good faith. But see now *Stone v. Ritter*, 911 A. 2d. 362 (Del. S.C. 2006).

¹¹³ Hill & McDonnell, *supra* note 45 at 856, and that “[t]he stronger the structural bias, the weaker the showing of gross negligence would need to be.”

¹¹⁴ *Maxwell*, *supra* note 40 at para. 107.

¹¹⁵ Robert Flannigan, “The Adulteration of Fiduciary Doctrine in Corporate Law” (2006) 122 L.Q.R. 449 at 457.

the exercise of that power.¹¹⁶ Such an approach would be sensitive to the context in which the director obtained his appointment, the position he currently holds and the particular transaction being considered. A negligence standard is thus unnecessary as its chilling effect will result in independently minded directors being too cautious in generating corporate information, which can lead to too little useful information alongside too much irrelevant information. Other directors can, however, be shown to be reckless in exercising their powers of disclosure through proof of a failure to meet objective standards against a background of structural bias and conflicts of interest.¹¹⁷

In summary, a fraudulent standard of liability is apposite to both corporate and director liability (criminal/regulatory, but also civilly to investors, if any) in securities disclosure cases. The duty is to care, not to take care. But it is hard to envision the corporation as a separate entity when it comes to liability in insider type structures given the structural bias that exists in that directors often act in the interests of the major shareholder rather than the shareholders as a whole. Liability should attach to directors or controlling shareholders (as shadow directors if not more directly) or officers that in fact control the flow of information within the corporation, and who have abused the position they were in. To a large extent, however, existing securities actions outside of the U.S. by investors against issuers are thwarted by the need for each of them to prove reliance on the misstatements and the causal link between misstatement and loss (with the problem in Singapore having to also link loss and wrongdoer profit). Consequently, the concerns expressed above concerning issuer liability to compensate investors (as opposed to paying civil penalties to regulators) are at the moment largely a U.S.-centric problem. Our focus will now shift towards the corporate issuer being the plaintiff with the directors/officers/controlling shareholders the defendants. Even here, the argument made will be that fraud or recklessness should effectively be the standard of liability, despite the fact that directors owe extant duties of care and skill to the company.

V. INVESTORS SHOULD NOT BE PLAINTIFFS

A. *No Aggregate Loss within the Shareholder Constituency and Abusive Class Actions*

But if corporate information can affect different generations of shareholders differently, it could conceivably be argued that losing shareholders should still be allowed to seek compensation, if not from the issuer then someone else, like the directors.¹¹⁸ So, for example, in a case where a company has suffered losses from poor investments, it is the non-disclosure of those losses that creates problems from a securities law perspective as it favours existing shareholders at the expense of future shareholders, in that the former could sell their shares before disclosure and avoid a loss, and a new shareholder might buy in the period after the market had been misled and

¹¹⁶ Paul D. Finn, *Fiduciary Obligations* (Sydney: Law Book Co., 1977) at 3.

¹¹⁷ It could also be seen as a failure to meet standards of good faith peculiar to fiduciaries, see Richard Nolan & Matthew Conaglen, "Good Faith: What does it mean for fiduciaries and what does it tell us about them?" in Elise Bant & Matthew Harding eds., *Exploring Private Law* [forthcoming], at Ch. 15. [Good Faith].

¹¹⁸ Wan, *Reconsidering Personal Liability*, *supra* note 39.

take the loss that comes with the disclosure. It is quite clearly the investors who purchased at or after the time that disclosure should have been made who had, in fact, incurred financial losses.

The disclosure of the negative information is how the loss at the corporate level translates itself into a loss at the shareholder level which, due to the bifurcated structure of ownership created by the separate corporate form, is a complicated process, as we shall see. But, there may not in fact be any distinct shareholder loss as it could be a zero sum game amongst the investor community in that the positions of buyers and sellers net off.¹¹⁹ Further, John Coffee Jr. has argued that private securities litigation by shareholders against issuers for failing to satisfy continuous disclosure requirements served neither to deter nor to properly compensate investors because of the “circularity problem.”¹²⁰ The circularity problem is such that a diversified investor really only sees transaction costs¹²¹ in securities litigation against corporations as it is just as likely be an investor that is holding onto its shares and thus being indirectly a defendant, and one buying in after the point in which proper disclosure (we are assuming the withholding of bad news here) should have been made, where they form part of the plaintiff class.¹²² More relevantly, perhaps, with some diversified investors more likely to hold than to trade (and holders have no standing to sue), they may end up more often having to indirectly pay out to trading investors than they receive. Worse, even where they did buy in at the relevant time, and so may be part of a plaintiff group, their propensity to hold may mean that they may not be able to prove a causative loss as they would not have sold by the time the action is brought or settled, and we have seen that this may now be required of plaintiffs in U.S. 10b-5 cases.¹²³

But compensation for a particular class of investors, particularly undiversified ones, can be justified if there are good reasons for it. And even if compensation fails as a rationale, there is still the deterrence argument. As we have seen, Fox has argued that private securities litigation to enforce disclosure is intended to enhance corporate governance and is less about investor protection.¹²⁴ He thought that disclosure also reduces the disclosing entity’s cost of capital as transparency increases liquidity for the company’s shares. So investors benefit from disclosure indirectly through better corporate governance and higher stock liquidity. Fox argued that the cost of private securities litigation that is ultimately borne by them is thus a fee that they have to bear for the enhancement of corporate disclosure and governance.¹²⁵ Still, he recognised that private securities litigation in the form of actions by investors against issuers was really a second best solution to create private deterrence—his preference discussed

¹¹⁹ Fox, *Why Civil Liability for Disclosure Violations*, *supra* note 15 at 302.

¹²⁰ Coffee, *supra* note 41 at 1556-1561. Or “circuitry” problem: James D. Cox, “Making Securities Fraud Class Actions Virtuous” (1997) 39 *Ariz. L. Rev.* 497 at 509.

¹²¹ Legal fees alone amount to US\$2.5 billion a year: see Fox, *Why Civil Liability for Disclosure Violations*, *supra* note 15 at 306-307.

¹²² Richard A. Booth, “The Future of Securities Litigation” (2009) 4 *J. Bus. Tech. L.* 129 at 139-140 [*Future of Securities Litigation*]. They may also be lucky sellers exiting during the class period when shares were overvalued.

¹²³ See *supra* note 71 *et seq.* and accompanying text.

¹²⁴ Fox, *Why Civil Liability for Disclosure Violations*, *supra* note 15 at 318, and Fox, *Civil Liability and Mandatory Disclosure*, *supra* note 20 at 253.

¹²⁵ Fox, *Why Civil Liability for Disclosure Violations*, *supra* note 15 at 327-328.

below was for reform to permit issuers to be plaintiffs and for directors and officers, as well as third party intermediaries, to be the defendants.¹²⁶

Fisch on the other hand argues for a broader conception of investor protection, one which enhances price efficiency in the markets and hence helps to discipline corporate managers. It is consistent with Goshen and Parchomovsky's point about the aim of securities regulation¹²⁷ which is that acquiring information is costly and the law tries to lower that for professional investors (Fisch prefers "informed traders").¹²⁸ Disclosure, in particular, reduces their search costs and so makes them willing to pay more for the shares. Informed investors trade on firm specific information unlike diversified investors and they are more affected by fraudulent information — so they suffer a "special damage" of sorts. But this then impacts both on the company, as well as existing shareholders, whose payment of damages is the fee they bear to encourage informed investors to do their job properly. But distinguishing informed traders from uninformed traders may be difficult in practice as the latter would often also claim reliance on the fraudulent information. Thus, while Fisch thought that this deals best with the circularity problem highlighted above, she asks for a "reformulation" of the fraud on the market approach in private securities litigation.¹²⁹

But a more fundamental objection to her argument which Fisch acknowledges is that gains and losses in securities actions by investors are not neutral in that longer term investors that hold may have to pay out to short term investors, who because of frequent trades are likely to buy and to have sold by the time the company has to pay out.¹³⁰ So stated the zero sum game is systematically rigged in favour of one particular group or generation of shareholders who stand to win over time from the inter-generational conflict.¹³¹ There would be enormous political difficulties in compensating trading investors like hedge funds at the expense of holding investors such as pension funds under these circumstances.¹³² The public will, at the least, cry foul at the likely abuse by the winners in such a system, even if the differences between such funds are possibly much less than is often perceived.¹³³

B. Company as the Proper Plaintiff—Damage?

Separately, Fox has argued even more fervently about the social value of disclosure, regardless of whether the issuer is selling new shares at the same time.¹³⁴ He has

¹²⁶ *Ibid.* at 332.

¹²⁷ This is adapted from Jane Stapleton, "The Gist of Negligence" (1988) L.Q.R. 213, and discussed below at text accompanying note 139. But Goshen & Parchomovsky, *supra* note 1, argue for an extension of the fraud on the market presumption to cases other than those where information is injected into an efficient market, and also for there to be negligence liability.

¹²⁸ Fisch, *Confronting the Circularity Problem*, *supra* note 58 at 345. See also Easterbrook and Fischel, *supra* note 21 at 689.

¹²⁹ Fisch, *Confronting the Circularity Problem*, *supra* note 58 at 349.

¹³⁰ *Ibid.* at 348, and Fisch, *Cause for Concern*, *supra* note 70 at 871.

¹³¹ See *supra* note 53.

¹³² Fisch, *Confronting the Circularity Problem*, *supra* note 58 at 348.

¹³³ Lawrence Mitchell, "Protect industry from predatory speculators" *Financial Times* (8 July 2009) points out that, today, even pension funds actively trade, with a 90% turnover compared to mutual funds (110%) and a general market turnover of 120%.

¹³⁴ Fox, *Civil Liability and Mandatory Disclosure*, *supra* note 20 at 268-269.

proposed a civil liability regime that is just as strong in enforcing corporate disclosure regardless of whether any fundraising is occurring at the same time. While there is issuer liability where it offers new shares for subscription or purchase, he argues that the basic private civil liability system in all instances should be one that provides for corporate actions against individual wrongdoers and third parties like investment banks. This proposal avoids the criticism above, *i.e.*, that traders win at the expense of holders, which is a drawback with investor actions, although arguably both sets of investors could have already priced this into their respective valuation of securities.

From a corporate law perspective, however, Booth has argued that derivative actions are more appropriate for securities fraud actions but that directors should be liable only when they make a gain which would in effect limit it to insider trading (at least at the federal level).¹³⁵ And in a more recent article,¹³⁶ he argues that in the case of many direct class actions brought by investors under 10b-5, the losses claimed for are often more in the nature of corporate losses, and investors should have claimed for them through a derivative action. This is true in the case of the fundamental loss that forms the basis of the bad news, that is, the underlying loss suffered by the business, which is not actionable as it is not a disclosure problem. But it is also true of capitalisation loss (change in earnings multiplier) which is the reputational damage resulting from the series of poor disclosures and the increased difficulty in accessing the capital markets, which was Fox's concern. And in the case of feedback loss, which is caused to the corporation by the litigation which shareholders derive their loss from, that disappears if class actions cannot proceed on the capitalisation loss. In the end, he feels that it is for the U.S. courts to rectify the problem since the classification of an action is within their purview, and the securities fraud class action there was really court created.¹³⁷

But it is possible to argue that issuer corporations can still prove a recoverable loss (other than the fundamental loss which may have been the result of a different breach of duty) even where the wrongdoing insiders do not make a gain from fraudulent disclosures. There is, at the least, the reputational damage suffered by the corporation, although that may be hard to quantify. In Singapore, however, *Vita Health*¹³⁸ provides an interesting remedial solution. The managing director's wrong in this case consisted of misstating the accounts and this painted a positive picture of the company in order to attract outside investors to buy his shares. The court held, however, that the company itself was also entitled to substantial damages against the managing director even though the losses were not in fact suffered by the company. Because of his fraudulent conduct, the managing director was bound to the

¹³⁵ Booth, *Future of Securities Litigation*, *supra* note 122. See also Richard A. Booth, "Direct and Derivative Claims in Securities Fraud Litigation" (4 May 2009), Villanova Law/Public Policy Research Paper No. 2009-11, online: <<http://ssrn.com/abstract=1398935>> at 20-22, acknowledging that misappropriation at state level is a wider concept and may extend to gains obtained other than through insider trading.

¹³⁶ *Ibid.* at 8-10.

¹³⁷ *Ibid.* at 22-29. 10b-5 actions are brought under the *Securities Exchange Act 1934 (U.S.)*, s. 10(b), which applies generally to any misstatement or omission of material information. *Blue Chips*, *supra* note 70, restricts 10b-5 claims to plaintiff buyers or sellers during the fraud period, but Booth argues that the corporation can bring the claim as its stock has been bought or sold, even if has not done so itself, or that *Blue Chips* does not apply to a derivative claim.

¹³⁸ *Supra* note 2.

misleading picture he had created in inducing shareholders to buy into the company. Equity, in a sense, deemed done that which ought to be done. The amount claimed at the corporate level would then feed into share prices in a manner determined by investors.

In *Vita Health*, Rajah J.C. (as he then was) utilised the remoteness rules in *Doyle*,¹³⁹ *i.e.*, that a wrongdoer is liable for all the losses resulting from a fraudulently induced transaction, including consequential losses. Foreseeability is not necessary in this instance. Unlike recent U.S. securities fraud on the market cases, nothing was said about a more stringent loss causation test, which could mean that intervening factors like a general market collapse, which in today's financial markets is in truth always foreseeable, would not prevent full recovery.¹⁴⁰ But this is right for, as Kumaralingam Amirthalingam has argued in a different context, damages should sometimes be payable where the wrongdoer has created an unacceptable risk for which he should be liable,¹⁴¹ where evidential difficulties make it impossible to prove the chain of causation connecting the wrong to the harm. While that was in the context of negligence in the modern post-industrial world, where such an approach is highly controversial, the important recent medical negligence decision in *Surender Singh s/o Jagdish Singh v. Li Man Kay*¹⁴² has applied what Amirthalingam termed the "formerly discredited approach"¹⁴³ in *McGhee v. National Coal Board*¹⁴⁴ in finding that there was a sufficient causal connection where the defendants' act "made the risk of death to the Deceased more probable."¹⁴⁵

The argument for such a liberal causation rule in the case of fraud is less controvertible, and in *Vita Health* it was not complicated by the need to define loss at the shareholder level. But although the claim is at the corporate level, it is for the serious risk of shareholder losses resulting from corporate misstatements. But this ultimate harm is hard to quantify or sometimes even conceive of and so the focus should be on the intermediate harm (which are the risks from the overstatement).¹⁴⁶ The harm is to corporate governance and reputation, and instead of asking about reasonable foreseeability, the question is the form or level of recovery that is reasonable.¹⁴⁷ Framed in such a way, it was clearly reasonable that the wrongdoer was held to the misstatements as if they were true. Such a technique has been used to make a fiduciary hold a bribe on constructive trust.¹⁴⁸ But it is policy laden, as

¹³⁹ *Supra* note 90.

¹⁴⁰ In most cases, loss causation and remoteness are treated as one under a directness test, although the conflation is criticised by von Jenner, *supra* note 66 at 12. See also Alexander Loke, "Adequate and just compensation for fraud-induced acquisition of shares" [1997] Sing. J.L.S. 318 at 324 [*Adequate and Just Compensation*].

¹⁴¹ Kumaralingam Amirthalingam "The Changing Face of the Gist of Negligence" in J. Neyers, S. Pitel, E. Chamberlain, eds., *Emerging Issues in Tort Law* (Oxford: Hart Publishing, 2007). See also *supra* note 83 *et seq.* and accompanying text.

¹⁴² [2009] SGHC 168 [*Surender Singh*].

¹⁴³ *Amirthalingam, supra* note 141 at 470.

¹⁴⁴ [1973] 1 W.L.R. 1 (H.L.).

¹⁴⁵ *Surender Singh, supra* note 142 *per* Lai Siu Chiu J. at para. 240.

¹⁴⁶ *Amirthalingam, supra* note 141 at 483.

¹⁴⁷ *Ibid.* at 485.

¹⁴⁸ *Attorney General of H.K. v. Reid* [1993] A.C. 713, applied in Singapore in *Kartika Ratna Thahir v. Pertamina* [1994] 3 S.L.R. 257 (C.A.).

Rajah J.C. observed:

In assessing damages for fraud, a mechanical approach is to be eschewed in favour of flexibility. The multi-faceted dimensions of fraud require pragmatism and malleability from the court in fashioning the appropriate remedy. Creative accounting may require creative remedies. While the deterrent factor may sometimes be cloaked in an award of damages, it should not be forgotten.¹⁴⁹

But such flexibility is not unusual in the case of fraud claims. Rajah J.C. acknowledged that in deciding on the time at which to assess damages, the House of Lords in *Smith New Court Securities Ltd. v. Scrimgeour Vickers (Asset Management) Ltd.*¹⁵⁰ had previously rejected a strict “date of transaction” approach based on the difference between the price paid and value of shares received on the date of the transaction. Instead, the House applied the general test for fraud, where the loss does not have to flow from the falsity of the misrepresentation, which provided it greater leeway. Approving of Lord Steyn’s speech in that case, Rajah J.C. thought that his Lordship “took pains to stress the importance of deterrence as a policy consideration in assessing damages for fraud. Intentional torts are rightly singled out for special consideration.”¹⁵¹ It is therefore a matter of policy that there could be a stricter loss causation requirement in the case of shareholder actions for disclosure fraud, which are difficult to quantify and are brought against issuers (and their shareholders) that do not benefit from the fraud, than at the corporate level where the claim is brought against persons who may benefit from the wrong, and even if not, are directly responsible for it. It attests to the different kinds of wrong and harm that are recognised in society where, with fraud, the goal is perhaps more, or at least as much, deterrence as compensation.¹⁵²

C. Directors as Defendants—Why not Negligence Liability?

Vita Health suggests that in Singapore, corporate disclosure can be enhanced through the enforcement of extant directors’ duties to act *bona fide* in the best interest of the company which are owed to the company. Here, what good faith really means is that the fiduciary cannot exercise powers of disclosure that have been vested in him in bad faith.¹⁵³ But it was argued above that fraud or recklessness is the preferred standard for criminal liability, regulatory penalties or investor civil claims as cases like *Wang Ziyi Able* have developed a basis for using evidentiary burdens to prove the necessary intent and are thus more nuanced and predictable. This may not be the case with the good faith duty where subjective dishonesty has usually been found to be required for there to be bad faith, unlike the more objective obligation imposed

¹⁴⁹ *Vita Health*, *supra* note 2 at para. 93.

¹⁵⁰ *Smith New Court Securities Ltd. v. Scrimgeour Vickers (Asset Management) Ltd.* [1997] A.C. 254 [*Smith New Court*].

¹⁵¹ *Vita Health*, *supra* note 2 at para. 92.

¹⁵² In his comments on *Smith New Court*, Loke, *Adequate and Just Compensation*, *supra* note 140 at 326, cogently argues that it is no longer “a factual causation question. Rather it is a question of legal policy motivated by the moral dimension of the law of torts and the deterrent policy it serves.”

¹⁵³ Richard Nolan, “Controlling Fiduciary Powers” [2009] C.L.J. 293 at 295-296 [*Controlling Fiduciary Powers*].

on directors to, for example, exercise their powers for proper purposes,¹⁵⁴ which is another technique Richard Nolan identifies as having been used to control fiduciary powers.¹⁵⁵ It has also been argued elsewhere how the good faith duty on directors in Singapore has been influenced by the hands off or no second-guessing approach courts take to business decisions without clear exposition of how it interacts with the objective duty of care and skill, and that in contrast the proper purpose rule could serve as the basis for a duty of disclosure, though there owed to present and future shareholders.¹⁵⁶ But this then compels us to ask why it is not enough to rely on extant duties of care and skill where it is just the company bringing an action against directors or individual wrongdoers for disclosure violations?¹⁵⁷

The arguments made above as to why the fraud standard of liability was apposite for criminal, regulatory or investor actions are still relevant here, namely that there would be a chilling effect on directors and officers were negligence to be the standard of liability in actions that are brought by their companies against them, even though this is likely for sums much smaller than in the case of investor class actions (given the U.S. experience). This would be particularly true of independent or outside directors. It is possibly for this reason that section 463 of the *Companies Act 2006 (U.K.)* makes a director liable to the company for misstatements in the directors' report, remuneration report or summary financial statement derived from either of these reports only in the case of fraud (knowledge or recklessness). This can be seen as some form of business judgment rule protecting directors from negligence liability (which jurisdictions like the U.S., Australia and Malaysia have recognised as applicable to directors' duties generally but which Singapore, like the U.K., does not have in its true form as opposed to a deferential approach taken towards decisions of directors discussed in the previous paragraph).¹⁵⁸ This though creates some form of safe harbour only in the specific context of certain financial disclosures.

Yet, with the insider directors, recklessness can be proved by showing gross negligence against a background of structural bias, where directors are in a position where they are likely to act against the corporate interest and in favour of another constituency,¹⁵⁹ which would be the major shareholder in a closely-held company. The point has been made that courts can discern a breach of the duty of loyalty far more easily than they do the duty of care. In the case of listed companies, it has been suggested that it should be left to professional analysts, aided by mandatory

¹⁵⁴ Austin J. at first instance in *ASIC v. Vines* [2005] 55 A.C.S.R. 617 at para. 1099 (Federal Court). In *Fulham F.C. v. Tigana* [2004] EWHC 2585 at para. 103, Elias J. (whose decision was affirmed by the Court of Appeal in [2005] EWCA Civ. 895), stated that "the fiduciary obligation requires him to disclose what he considers—not what the court may consider—is in the interests of the company."

¹⁵⁵ Nolan, *Controlling Fiduciary Powers*, *supra* note 153 at 297-304.

¹⁵⁶ The cases highlighted at *supra* note 2 are discussed in Tjio, *Rationalisation of Directors' Duties*, *supra* note 53, where it was argued that the duty to act constitutionally and for proper purposes (now encapsulated in the *Companies Act 2006 (U.K.)* s. 171) could serve as the basis for the duty of disclosure. While that could capture the essence of disclosure, which is to enhance corporate governance, fraud or recklessness as the standard of liability allows better enforcement of the duty by coming at it from the other side of the equation. It can also be applied more readily to controlling persons that are not fiduciaries.

¹⁵⁷ The *H.M. Treasury*, *supra* note 4 at para. 7.10, accepted Paul Davies' recommendation that issuer actions against directors for negligence should be left to the common law.

¹⁵⁸ Tjio, *Rationalisation of Directors' Duties*, *supra* note 53.

¹⁵⁹ Hill & McDonnell, *supra* note 45.

disclosure rules, to monitor the duty of care.¹⁶⁰ The courts' comparative advantage is in picking up more culpable wrongdoing. A limited business judgment rule for directors in the context of financial disclosures would also be consistent with the joint and several liability that could attach to controlling shareholders under section 20(a) of the *Securities Exchange Act 1934 (U.S.)*, which applies "unless the controlling person acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action." With controlling shareholders, therefore, a provision may be needed to create a duty of good faith, whereas in the case of directors, section 463 of the *Companies Act 2006 (U.K.)* serves to restrict the application of extant negligence liability which could otherwise lead to the production of too little useful, and too much superfluous, information.

In any case, negligence liability may not help in the *Vita Health* situation as it was the bad faith finding of Rajah J.C. that led to the very favourable causation rules which permitted the company to show that it had suffered a loss. The reality is that in many cases of misleading or delayed disclosures, the company would find it difficult to quantify its loss under traditional causation principles since the disclosures impact on share prices more directly. We have seen that Booth identified the capitalisation loss or reputational damage suffered by the company as the main avenue of recovery but even he was careful to advocate restricting issuer claims to profits made by the wrongdoing directors.¹⁶¹ An account of profits is usually only available where there is a breach of a statutory or equitable right. Equitable fraud must also be present for the technique used in *Vita Health* to work, viz. that the wrongdoer is held to the truth of the misstatements that he made, which can be seen as a way of redressing the reputational harm suffered by the company. But such harm is created far more evidently by directors acting in an egregious manner than where they are merely negligent. Consequently, while it may seem like the tail wagging the dog, the whole basis of corporate recovery in the context of disclosure violations is based on fraud or recklessness on the part of directors, officers or controlling shareholders and its remedial consequences are inextricably tied up with, and, in turn influences, the applicable standard of liability.

In *Maxwell*¹⁶² it was held that a director was not criminally liable for breaches of his statutory duties of care and skill (and good faith) due to the misleading and deceptive conduct by the corporation (as well as breach of the prospectus rules) in raising funds without a disclosure document. The court said that he had not made any statement referring to an offer of securities that could be attributed to him¹⁶³ and thought that the statutory provisions on directors duties (largely an expanded version of section 157 of the *Companies Act (Singapore)* that is presently being considered in Singapore),¹⁶⁴ while it did not require a formal proof of damage to the corporation, still required that there was foreseeable risk that the directors' act or omission might harm the corporation. Both the duties of care and good faith are not duties about

¹⁶⁰ Goshen & Parchomovsky, *supra* note 1.

¹⁶¹ Booth, *Future of Securities Regulation*, *supra* note 122.

¹⁶² *Supra* note 40.

¹⁶³ *Ibid.* at para. 124.

¹⁶⁴ It appears that the Singapore Government will take a wait and see attitude to how the codification of directors' duties in the UK, and the statutory formulation in Australia (which is not exhaustive), will pan out: see The Steering Committee for Review of the Companies Act, Discussion Paper 1, "Directors" (1 August 2009) para. 80 [*Steering Committee for Review of the Companies Act*].

behaving well in the abstract, but doing well by the company,¹⁶⁵ and as such it is difficult to envisage meaningful negligence liability on the part of directors in the context of a disclosure violation where it can be shown that the company suffers a recoverable loss. It is easier in the context of good faith, especially in its bad faith formulation, where the company's image is tarnished by the recklessness of its directors. It is perhaps for this reason too that in cases of fraud which impacts on a company's outside dealings, it appears that only the state of mind of the company's directing mind and will is attributed to it, and not that of an officer that is otherwise attributed to the company in non-fraud situations.¹⁶⁶ This is because an officer's fraud in relation to a third party is also one against the company.

Often, it is also the case that the relevant misstatement or non-disclosure involves a risk or forward-looking statement, and not a known event. At common law, it has always been held that only statements of fact, not opinion or future intention, are actionable. It is only if that opinion or intention is not honestly held that the law intervenes.¹⁶⁷ But the relevant information may relate to past events, and are clearly then statements of fact that are actionable *per se*. Even here, however, it can be argued that corrective disclosure has hard-to-determine causative effects on the market given that it would have to be ascertained "how disclosure of the omitted or misrepresented information would affect investor beliefs regarding the magnitude of future cash payouts and the likelihood of receiving those payments."¹⁶⁸ Directors and officers would be wary about how their statements are interpreted given the usual rumours in the market, some of which would have already fed into the share price. Directors may therefore be trying to see when and how disclosure could be made in a way that impacts least on the shareholder community (present and future, and sometimes even other constituencies like employees) in a way that fulfils their duty to exercise their powers in an even-handed way. Too much liability would lead to overly defensive reporting. This may explain why on 10 March 2009, Neptune Orient Lines ("NOL") declined to comment when queried whether it was intending a rights issue as had been suggested in a Dow Jones report. Its share price continued to fall until it unequivocally denied plans of a rights issue three days later. For this it received a public reprimand from the SGX.¹⁶⁹ While this may have been appropriate, civil liability, which exists somewhat further up the hierarchy of sanctions, may not be unless fraud was present, or there was some kind of insider activity in the market which accompanied the rumours. NOL's board was placed in a difficult position given the speculation and the worldwide market sentiment at that time. It might not have been a position yet to deny the rumours outright, but could have said that there was only a possibility or probability of there being a rights issue or not, as the case may be. But this information was already circulating in the market. It is therefore not clear that a vague holding reply, if made in good faith, should be actionable given that

¹⁶⁵ Maxwell, *supra* note 40 at para. 102.

¹⁶⁶ *In re Hampshire Land Company* [1896] 2 Ch. 743, but compare *Lloyd v. Grace, Smith & Co.* [1912] A.C. 716. See now *Moore Stephens*, *supra* note 110.

¹⁶⁷ *Edgington v. Fitzmaurice* (1885) 29 Ch. D. 459 (C.A.).

¹⁶⁸ Bradford Cornell & R. Gregory Morgan, "Using Finance Theory" (1990) 37 U.C.L.A. L. Rev. 883 at 895.

¹⁶⁹ See R. Sivanithy, "Deter Disclosure Lapses with Fines" *Business Times* (19 March 2009); Lynette Khoo, "Why did NOL get rapped while Capitaland did not?" *Business Times* (21 March 2009).

the investors attached their own assessments as to the mathematical chances of the relevant event occurring. These corporate statements are not made in a face-to-face or one-to-one situation but are made to a diverse market ready to pounce on every word.

In brief, it has been argued that a duty of disclosure founded on negligence liability is not appropriate if the goal is to generate useful corporate information. There are many instances in practice where the officers of a company have to take a good faith business decision not to disclose information for reasons such as its incipient nature, or conversely, they may take a considered decision to disclose such information because of the fear of a false market developing which later turns out to be premature. Corporate actions against directors for bad faith or recklessness, however, are a better fit, given that courts in Singapore have also defined corporate harm resulting from intentional torts quite broadly, which is consistent with most fraud claims. In the case of directors, there is a need to offer some form of safe harbour from negligence liability in the context of financial disclosures along the lines of section 463 of the *Companies Act 2006 (U.K.)*. This would then, in effect, make it less of a duty to disclose timeously and accurately, and more a power to disclose that cannot be abused as discussed earlier. In the case of controlling shareholders that do not owe any extant duty of care to the company, however, a statutory provision may be required to establish a standard of liability where they are party to a disclosure violation. Here, not being fiduciaries, any applicable good faith formulation is different in that while regard must be had to the company's interest, such persons are not expected to systematically prioritise it.¹⁷⁰ So a clear rule based on the fraudulent or reckless disregard of the continuous disclosure rules would be useful.

VI. CONCLUSION

The gist of securities litigation to enforce corporate disclosure is the deterrence of a director or officer from creating an unacceptable risk to shareholders by being reckless with the powers of disclosure vested in him, given the reach and difficulties of ascertaining the effects of breaches of that power. It is to prevent the fraud or improper use of that power. This can be proved by background evidence showing his links to the major shareholder or another constituency, in circumstances where he cannot explain why he did not do what the reasonable director or officer in his position would have. The use of objective facts to prove subjective intent is a broader application of *Wang Ziyi Able* where fraud or recklessness was considered in the narrower confines of section 199 of the *Securities and Futures Act (Singapore)*.¹⁷¹ For such an act or omission in relation to the power given to him to disclose corporate information, a director is liable for the loss "suffered" by the corporation on a generous causation or remoteness rule drawn from common law fraud. The important authority here for us is *Vita Health*.¹⁷² However, it may not be enough to leave it to common law directors' duties alone, with negligence being too wide and needing a limited

¹⁷⁰ Nolan & Conaglen, *Good Faith*, *supra* note 117.

¹⁷¹ See *supra* note 103 *et seq.* and accompanying text.

¹⁷² See *supra* note 139 *et seq.* and accompanying text.

business judgment rule in the context of financial disclosures. At the same time, the private enforcement of continuous disclosure would be facilitated by statutorily encapsulating the need for controlling shareholders to make disclosure properly. What should also be considered is the widening of section 216A of the *Companies Act (Singapore)* to allow statutory derivative actions to be brought in the case of publicly listed companies, which is now the position in many jurisdictions around the world.¹⁷³

The problem remains that in the current environment where investors can sue directors and officers, in the U.S. under 10b-5 and elsewhere at common law (which this article has argued should not be the primary mode of private enforcement), with Director and Officer (D&O) insurance, “little liability remains with the directors.”¹⁷⁴ This should be less of a problem in cases where the company brings an action against its directors and officers for fraud as the corporation is most cognisant about the indemnity and insurance arrangements within the corporate structure to see if a suit is advantageous.¹⁷⁵ Even so, Fox has suggested for his proposed civil liability regime in which the issuer is the plaintiff, only litigation fees should be payable by insurers,¹⁷⁶ and no other indemnification or insurance of the directors and officers be allowed otherwise. But this would necessitate a major change to section 172(2) of the *Companies Act (Singapore)*, which presently allows liability insurance (but it is less clear about insurers providing upfront payments of litigation fees),¹⁷⁷ as well as corporate indemnities (although there is some uncertainty over whether this can cover third party claims).¹⁷⁸ Changes could also be made to prevent indemnification or insurance only in derivative or corporate actions against the directors and officers, but this could be seen as still too much interference with market forces, as the terms of insurance are usually quite freely negotiated.¹⁷⁹ Perhaps the easiest statutory

¹⁷³ *Tjio & Wee*, *supra* note 59 at 339-340.

¹⁷⁴ Davies, *Review of Issuer Liability*, *supra* note 81 at para. 102. See also Boros, *Shareholder Litigation after Sons of Gwalia v Margaretic*, *supra* note 75 at 247 regarding the Australian position. For the U.S. position, see Coffee, *supra* note 41 at 1550-1554, stating that in almost all cases, “the corporate defendant and its insurer advance the entire settlement amount.” Even if directors are sued, they seldom pay.

¹⁷⁵ Davies, *Final Report*, *supra* note 4 at para. 57, linking it to the new statutory derivative action created in England by *Companies Act 2006 (U.K.)*.

¹⁷⁶ Fox, *Civil Liability and Mandatory Disclosure*, *supra* note 20 at 287.

¹⁷⁷ Contrast the U.K. position, which was amended by the *Companies (Audit, Investigations and Community Enterprise) Act 2004* to provide, *inter alia*, further relief to directors by allowing companies to assist their directors financially while litigation is proceeding, *even where the action is taken by the company itself*, but subject to clawback if the director is found liable or is convicted.

¹⁷⁸ See *Steering Committee for Review of the Companies Act*, *supra* note 164 at Part XIII. The proposal is to amend *Companies Act*, s. 172(2)(b) to allow corporate indemnities in the case of third party claims, subject to certain restrictions, and also to allow indemnities covering potential liabilities. A similar restrictive interpretation does not appear to have been taken with respect to insurance arrangements under s. 172(2)(a).

¹⁷⁹ The 2004 changes in the U.K., italicised at *supra* note 177, show that the starting point is that the company can provide insurance or indemnity cover even for actions it initiates against its directors and officers, and that seems clearly to be the position in Singapore: see *Steering Committee for Review of the Companies Act*, *supra* note 164 at Part XIII. However, the Australia Companies and Securities Law Review Committee, *Company Directors and Officers: Indemnification, Relief and Insurance* (April 1999) [Australia Companies and Securities Law Review Committee] at para. 162 points out that the archetypal director and officer policy in Australia at that time excluded coverage where the claim is brought by the company. Other situations in which a policy excluded liability were where a director

change would be to clearly deny indemnification or insurance in cases of fraud or recklessness, which would be consistent with the structure and standard of liability advocated here (liability insurance could presently cover fraud, and even if not, so long as the director does not admit liability, a claim for fraud could still be settled with the insurer paying).¹⁸⁰ Again, this is an argument resting on the fact that the consequence of a liability standard is so closely intertwined with it that it buttresses the argument for that particular standard. Here, given the widespread use of insurance and indemnity arrangements, there can be no meaningful negligence liability for disclosure violations by directors unless we, in effect, completely abrogate the relevant insurance and indemnity provisions in section 172(2) of the *Companies Act (Singapore)*.

While, often, directors and officers do not have deep pockets, and in fact Fox's proposed civil liability system would cap their liability to their levels of compensation,¹⁸¹ the aim is less compensation than deterrence. So it is how the directors and officers are affected that matters from a corporate governance perspective, and not the levels of investor recovery. This also deals with a second "circularity" problem if the defendant director/officer is also a substantial shareholder, since the indirect benefit he obtains through issuer recovery is always proportionately less than what he has to pay out in damages. But in insider type companies, it is important that the directors and officers actually pay something, as they are unlikely to suffer other setbacks such as loss of office that might accompany their making of false and misleading corporate statements in outsider type companies.¹⁸² The present position in such companies in the U.S. is quite the opposite—issuer liability with a large part of that borne by insurance. We should be conscious that many there do not see this as an optimal solution as we try to improve our corporate governance regime, particularly where disclosure is concerned, in order to make private enforcement supplement the criminal sanctions and civil penalties sought by the state.

made a personal profit or where the loss was caused by "dishonest, fraudulent, criminal or malicious ... wilful or reckless" acts of a director.

¹⁸⁰ Davies, *Review of Issuer Liability*, *supra* note 81 at para. 101. Compare his *Final Report*, *supra* note 4 at footnote 43. In the U.S., insurance will not cover cases of "deliberate fraud", which is why cases are settled with issuers paying rather than for actions to proceed against the directors and officers since actions against the latter are more likely to indicate serious moral turpitude. But it could be argued that *Companies Act*, s. 172 should similarly not cover fraud or recklessness since it only refers to the company purchasing insurance against liability in respect of "negligence, default, breach of duty or breach of trust." However, the same language is used in *Companies Act*, s. 391 in terms of the court's discretion to relieve a director from liability, and it has been recognised that they are related provisions: *Australia Companies and Securities Law Review Committee*, *ibid.* at 97. In Singapore, it has been held that *Companies Act*, s. 391 does not include only breaches of trust that involved a misappropriation of trust property: *Hytech Builders Ptd. Ltd. v. Tan Eng Leong* [1995] 2 S.L.R. 795 (H.C). Other breaches of trust are covered, and it has also been argued that breaches of fiduciary duty should be included: Pearlie Koh, "An Issue of Absolution: Section 391 of the Companies Act" (2003) 15 S.Ac.L.J. 306. The position is not fully settled as it appears that there are fraudulent and non-fraudulent breaches of fiduciary duty: see Evans L.J. in *Swindle*, *supra* note 89.

¹⁸¹ Fox, *Civil Liability and Mandatory Disclosure*, *supra* note 20 at 288.

¹⁸² See Mak Yuen Teen, "See Hup Seng's retaining of tainted CEO short-sighted" *Business Times* (9 September 2008), querying the company's action in light of his fine for insider trading.