DIRECTORS' LIABILITY AND CLIMATE RISK: WHITE PAPER ON SINGAPORE

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About the Commonwealth Climate and Law Initiative (CCLI)

The CCLI is a legal research and stakeholder engagement initiative founded by Oxford University Smith School of Enterprise and the Environment, ClientEarth and Accounting for Sustainability (A4S). The CCLI examines the legal basis for directors and trustees to manage and report on climate change-related risk and climate mitigation and our research is at the forefront of the intersection of climate and biodiversity risks under existing companies and securities laws. We also provide practical tools on how to integrate the risks and opportunities of climate change into corporate governance, to minimize the risk of personal liability and maximize efforts of the private sector in the transition to a sustainable economy. We convene conferences and stakeholder events to disseminate these messages and build capacity across the corporate, regulator and civil society ecosystem. Our aim is not to litigate, but to demonstrate that prevailing company laws and fiduciary duties compel action on climate change.

Founded to focus on four Commonwealth countries: Australia, Canada, South Africa, and the United Kingdom, the CCLI has expanded its remit to the United States, Singapore, India, Hong Kong, Japan and Malaysia. The CCLI leverages the inter-disciplinary and cross-jurisdictional perspectives provided by its global experts from academia and the legal, accountancy, business, and scientific communities. In Singapore, the CCLI is collaborating with the National University of Singapore.

The CCLI have commissioned a legal opinion on directors' liabilities and climate change from a team of counsel led by Jeffrey Chan Wah Teck SC. These publications will form the basis for education and stakeholder activities, such as workshops, events and engagement with financial regulators, investors and corporates. These activities will amplify the core message that Singaporean directors must consider climate change today in their governance and disclosure or risk liability in future.

About the author

Ernest Lim is an Associate Professor at the Faculty of Law, National University of Singapore (NUS). He obtained his D.Phil. and B.C.L. from Oxford, LL.M. from Harvard Law School and LL.B. from NUS. He has published widely on comparative corporate law and governance as well as private law. His books include *Sustainability and Corporate Mechanisms in Asia* (Cambridge University Press, 2020) and *A Case for Shareholders' Fiduciary Duties in Common Law Asia* (Cambridge University Press, 2019), which won the Society of Legal Scholars Peter Birks Prize for Outstanding Legal Scholarship (joint second prize). His third book is on comparative social enterprise. He is co-leading an international project on AI, the forthcoming output of which is *The Cambridge Handbook of Private Law and Artificial*

Intelligence. His peer reviewed articles have appeared or are forthcoming in the *Oxford Journal of Legal Studies*, *American Journal of Comparative Law*, and *Law Quarterly Review*. His work on corporate attribution in the *Modern Law Review* has been cited by the Singapore Court of Appeal and before the UK Supreme Court. He has been elected to the Robert S Campbell Visiting Fellowship at Magdalen College, Oxford. Prior to joining academia, he worked in the New York and Hong Kong offices of Davis Polk & Wardwell where he specialized in global capital market transactions.

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Disclaimer

I. INTRODUCTION

This white paper argues that in view of the well-established physical, transition and liability risks associated with climate change, and in light of the measures taken by the Singapore government and regulators to address these risks, directors of companies are required under Singapore law to take into account climate-related risks in their decision-making process, failing which they will be liable for breaching the duty to act in good faith in the best interests of the company and the duty to exercise reasonable diligence. Further, this paper shows that failing to disclose climate-related risks may amount to a breach of the Singapore Exchange's continuous disclosure requirements and the rules on sustainable reporting guide. Importantly, this paper also considers how the directors' duties can be enforced using the techniques of derivative action and oppression. To these ends, this paper complements and extends the analysis in the Chan Legal Opinion.

A. Climate change as a material financial risk

Climate change presents three major risks that do and continue to impact on companies, the broader economy and society. These risks can be categorized into three types: physical risks; transition risks; and liability risks.[1] Although the majority of these risks will materialize in the long-term, some will take place in the short to medium term. For example, assets of businesses that rely on or invest in fossil fuels will be stranded. Not only are the energy and resources sectors particularly vulnerable to climate-related risks, but so are the chemicals and manufacturing, agriculture, food and beverage, infrastructure, transport and logistics, and financial services sectors. Investors and regulators are particularly concerned about these risks given their systemic impact on the economy.

Physical risks include "changes in water availability, sourcing, and quality; food security; and extreme temperature changes affecting organizations' premises, operations, supply chain, transport needs, and employee safety."[2] For example, as has been forcefully and unequivocally articulated by the Singapore government[3], Singapore, a low-lying island, is acutely vulnerable to rising sea levels that can cause severe flooding and therefore, extensive

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[1] See for eg, TCFD, 'Final Report: Recommendations of the Task Force on Climate-related Financial Disclosures', June 2017, 26-7 <https://www.fsb-tcfd.org/publications/final-recommendations-report/>.

[2] Ibid, pg. 6.

[3] PM Lee, National Day Rally 2019 <https://www.pmo.gov.sg/Newsroom/National-Day-Rally-2019>.

destruction to properties and livelihoods; climate-risk poses an existential threat. The physical risks can also adversely impact companies in terms of reduction of future cash flow; increase in impairment or write-off of assets; increased provisions for contingencies; increased capital expenditure to protect supply chains operations and to repair property and equipment; and reduced revenue due to employees not being able to work.

Transition risks refer to the financial and reputational risks posed to organizations as a result of the legal, technological, and market changes brought about by the transition to a lower-carbon economy.[4] These changes include the laws, regulations and policies that are or will be adopted by the state and companies to address climate-related risks, a prominent example of which is reducing carbon emissions. Because Singapore has declared its intention to reduce its emissions by 50% by 2050 and its hope to achieve net-zero emissions by the second half of this century[5], transition risks will include the measures that have been and ought to be taken by the government and companies to attain this goal.

Liability risks refer to potential legal claims or regulatory proceedings to which companies and directors will be subject. These claims can arise from breaches of different statutes and regulations and violations of the common law. Although there appears to be no climate-related litigation involving shareholder derivative suits in Singapore companies, one cannot rule out the possibility there will be one in the future, in light of the increased litigation in other parts of the world[6] and to a certain extent in Asia.[7] For example, there are at least 1,587 climate-related lawsuits that have been filed. While most of the cases originated in the US, Europe and Australia, a minority come from Asian jurisdictions including the Philippines and Indonesia.[8] While the bulk of the lawsuits are related to public interest and public law litigation, there are instances of corporate litigation. For example, in 2018, a leading environmental NGO purchased shares in Enea, a Polish power company and successfully sued the company for participating in a project to build coal plants; the Polish court invalidated the resolution

4 Ibid, pg. 5.

5 National Climate Change Secretariat, *Charting Singapore's Low-Carbon and Climate Resilient Future* (2020), p 35 <https://www.nccs.gov.sg/docs/default-source/publications/nccsleds.pdf>.

6 Climate change litigation update, Norton Rose Fulbright (Feb 2020) <https://www.nortonrosefulbright.com/en-sg/knowledge/publications/7d58ae66/climate-change-litigation-update>.

7 Jolene Lin and Douglas Kysar, *Climate Change Litigation in the Asia Pacific* (CUP, 2020).

8 Setzer J and Byrnes R (2020) *Global Trends in Climate Change Litigation: 2020 Snapshot*. London: Grantham Research Institute on Climate Change and the Environment and Centre for Climate Change Economics and Policy, London School of Economics and Political Science <https://www.lse.ac.uk/granthaminstitute/publication/global-trends-in-climate-change-litigation-2020-snapshot/>.

approving the construction of the plant.[9] Finally, it cannot be ruled out that directors may be sued by the company for failing to take into account climate-related risks in their discharge of duties.

In view of the above risks, the Task Force on Climate-related Financial Disclosure (TCFD) (set up by the G20) made recommendations on voluntary disclosures related to climate risks in 2015 in order to raise awareness on the impact of these risks on the financial performance of companies and financial institutions (including banks, insurance firms and asset managers) and to ensure that the risks to individual firms are managed and mitigated, thus reducing the potential for system-wide shocks affecting financial stability.[10] The TCFD recommendations have been accepted by leading financial institutions and companies[11], and have been relied upon by shareholders to hold directors accountable for the way they have addressed climate-related risks.[12]

Further, in 2017, the Network of Central Banks and Supervisors for Greening the Financial System (NGFS), of which the Monetary Authority of Singapore (MAS) is one of the eight founders, was set up to manage risks and foster greater green and low-carbon investments.[13]

In 2020, the Government of Singapore Investment Corporation ("GIC"), Singapore's sovereign wealth fund, joined Climate Action 100+, an investor-led initiative which engages high-emission companies to reduce emissions of greenhouse gas, strengthen climate governance and enhance climate disclosure.[14]

Also, in 2020, the MAS urged financial institutions to report the impact of material climate-related risks on their business and operations in accordance with international guidelines

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9 https://www.clientearth.org/latest/latest-updates/news/major-court-win-shows-power-of-corporate-law-to-fight-climate-change/

10 n 1.

11 See eg, Sustainable Insurance Forum, 'Leading Insurance Supervisors Support Adoption of Climate Risk Disclosure Recommendations' (July 2017); Hamza Ali, 'Investors with $25trn of AUM back Climate Disclosures', Wealth Manager (29 June 2017) <http://citywire.co.uk/wealth-manager/news/investorswith-25trn-of-aum-back-climate-disclosures/a1029476#i=1>.

12 See eg, Joanna Partridge, "BlackRock votes against 49 companies for lack of climate crisis progress" Guardian (17 Sep 2020) <https://www.theguardian.com/business/2020/sep/17/blackrock-votes-against-49-companies-for-lack-of-climate-crisis-progress>.

13 https://www.ngfs.net/en.

14 "GIC aligns with CDP, Climate Action 100+, and AIGCC" <https://www.gic.com.sg/news-and-resources/gic-aligns-with-cdp-climate-action-100-and-aigcc/>.

including the TCFD recommendations.[15] The MAS has set out environmental risk management guidelines urging directors to:

- approve an environmental risk management framework and policies to assess and manage the financial institution's environmental risk exposures on an ongoing basis;
- ensure that material environmental risk is addressed within the financial institution's risk appetite framework;
- set clear roles and responsibilities for board members and senior management, including personnel who are responsible for overseeing the financial institution's environmental risk; and
- ensure adequate management expertise and resources for managing environmental risk, including thorough training and capacity building.[16]

Although these guidelines are not binding regulations (yet), responsible financial institutions cannot turn a blind eye to them. This is because these guidelines, issued by the most important financial regulator in Singapore, will become influential norms and will set the standard concerning how responsible financial institutions ought to address climate-related risks.

The MAS guidelines should not be understood in isolation. Rather, they reflect the increasing commitment by the Singapore authorities to hold financial institutions and companies accountable for their actions and omissions in relation to climate-related risks and more generally, environmental risks. For example, in 2016, the Singapore Exchange issued a set of listing rules to require companies on a comply or explain basis to furnish on an annual basis sustainability reports containing their identification and evaluation of material environmental, social and governance factors. Further, the Carbon Pricing Act was enacted in 2018 (to impose taxes in relation to greenhouse gas emissions) and the Resource Sustainability Act in 2019 (to impose obligations on companies with respect to the collection and treatment of waste).

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[15] MAS, "Guidelines on Environmental Risk Management (Banks)" (December 2020) <https://www.mas.gov.sg/-/media/MAS/Regulations-and-Financial-Stability/Regulations-Guidance-and-Licensing/Commercial-Banks/Regulations-Guidance-and-Licensing/Guidelines/Guidelines-on-Environmental-Risk---Banks/Guidelines-on-Environmental-Risk-Management-for-Banks.pdf>; MAS, "Guidelines on Environmental Risk Management (Insurers)" (December 2020) <https://www.mas.gov.sg/-/media/MAS/Regulations-and-Financial-Stability/Regulations-Guidance-and-Licensing/Insurance/Regulations-Guidance-and-Licensing/Guidelines/Guidelines-on-Environmental-Risk-Management-Insurers.pdf>; MAS, "Guidelines on Environmental Risk Management (Asset Managers)" (December 2020) <https://www.mas.gov.sg/-/media/MAS/Regulations-and-Financial-Stability/Regulations-Guidance-and-Licensing/Securities-Futures-and-Fund-Management/Regulations-Guidance-and-Licensing/Guidelines/Guidelines-on-Environmental-Risk-Management-for-Asset-Managers.pdf>.

[16] Ibid.

B. Brief overview of directors' duties

The law governing directors' duties in Singapore consists of both statutory law (principally but not exclusively the Companies Act (Cap 50)) and common law. Under Singapore law, directors owe fiduciary duties to the company which include the duty to act *bona fide* in the best interests of the company, the duty to avoid unauthorized conflicts of interest and unauthorized receipt of profits, and the duty to act for proper purposes. In addition, directors also owe non-fiduciary duties, the most important of which is the duty to exercise reasonable care, skill and diligence. The definition of directors in the Singapore Companies Act includes not only persons who have been formally appointed, but also those who have not been formally appointed but act as though they are directors as well as those whose directions or instructions the directors of the company are accustomed to act.[17] The consequence is that these persons are subject to duties under the Companies Act and the common law insofar as the statute reflects the common law.

C. Relationship between statutory and common law duties

The crucial provision for the purposes of this paper is s 157(1) of the Companies Act which provides: "A director shall at all times act honestly and use reasonable diligence in the discharge of the duties of his office." The duty to act honestly is the statutory equivalent of the common law duty to act in good faith in the best interests of the company.[18] And the duty to use reasonable diligence is a codification of the common law duty to exercise reasonable care, skill and diligence.[19] However, the statute does not supersede the common law because s 157(4) provides that "[t]his section is in addition to and not in derogation of any other written law or rule of law relating to the duty or liability of directors or officers of a company."

Thus, a director who is not in breach of s 157(1) may still be in breach of the common law such as the duty to act for proper purposes. Conversely, a director who is in breach of s 157(1) is not necessarily in breach of all the common law duties (because, for example, the director can be in breach of the statutory duty to exercise reasonable diligence but not the common law duty to act for proper purposes).

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[17] Section 4(1) Companies Act (Cap 50).

[18] *Townsing Henry George v Jenton Overseas Investment Pte Ltd (in liquidation)* [2007] SGCA 13 at [59].

[19] Ibid.

Further, it is important to note that a breach of s 157 entails criminal sanctions[20], unlike civil penalties in the case of breach of the common law duties.

Finally, the Companies Act imposes extensive disclosure obligations which are more onerous than or different from those imposed by the common law.[21]

II. THE DUTY TO ACT IN THE COMPANY'S BEST INTERESTS

A. Overview of common law duty

It is trite law that directors are required to act *bona fide* in the best interests of the company. There are thus two aspects to this duty: *bona fide* and best interests.

Regarding the *bona fide* aspect, it consists of subjective and objective elements, both of which must be satisfied.[22] The subjective element lies in the court's consideration as to whether a director had exercised his discretion *bona fide* in what he considered (and not what the court considers) is in the interests of the company. Thus, a court will be slow to interfere with commercial decisions made honestly but which, in hindsight, were financially detrimental to the company. As for the objective element, it "…relates to the court's supervision over directors who claim to have been genuinely acting to promote the company's interests even though, objectively, the transactions were not in the company's interests. The subjective belief of the directors cannot determine the issue: the court has to assess whether an intelligent and honest man in the position of a director of the company concerned could, in the whole of the existing circumstances, have reasonably believed that the transactions were for the benefit of the company … Thus, 'where the transaction is not objectively in the company's interests, a judge may very well draw an inference that the directors were not acting honestly'…"[23]

Under Singapore law, the objective element is not merely an exercise undertaken by the courts to test the veracity of the director's subjective assertion that the person has acted in good faith; rather it is a separate component according to which courts will exercise their supervisory powers over the directors' decision-making process. Accordingly, it is incorrect to characterize the best interest duty as principally a subjective duty; rather it is both a subjective and an objective duty. A director who has breached the subjective element will automatically breach

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[20] Section 157(3)(b): "…a fine not exceeding $5,000 or to imprisonment for a term not exceeding 12 months." See also section 156(15).

[21] See the disclosure of interests in transactions, property and offices requirements under s 156.

[22] *Goh Chan Peng v Beyonics Technology Ltd* [2017] SGCA 40 at [35]-[36].

[23] Ibid at [36].

the duty and a director who has complied with the subjective but not the objective element will also breach the duty.

Regarding what amounts to the best interests of a solvent company, there are three different conceptions of the interests of a solvent company:

- shareholder value;
- stakeholder value;
- and the corporate entity.[24]

The interests of a solvent company are often equated with long-term shareholder value, often defined in terms of share price or profitability.[25] However, corporate interest can and should also include stakeholders' interests. For example, Principle 13 of the Corporate Governance Code states that as part of the directors' duty to ensure that the best interests of the company are served, the board should adopt "an inclusive approach by considering and balancing the needs and interests of material stakeholders." A stakeholder interpretation of corporate interest is also supported by s 159(a) of the Companies Act which states that directors are entitled to have regard to the interests of employees and those of the members. By contrast, under s 172(1) of the UK Companies Act, which adopts an enlightened shareholder primacy model, directors are required to have regard to the interests of stakeholders but only as a means to benefit the shareholders. But Singapore law imposes no such requirement.

Finally, the court has recognized that the interests of a solvent company can mean the interests of the corporate entity itself, separate and distinct from those of shareholders and stakeholders.[26] For example, a decision by the board to plough back the profits into the company instead of distributing them as dividends to shareholders is consistent with the duty to act in the interests of the company defined as those of the corporate entity itself.[27] In other words, directors can prefer the interests of the corporate entity over those of shareholders.

B. Overview of statutory duty

Section 157(1) of the Companies Act requires directors to act honestly. This has been interpreted as being the equivalent of the common law duty to act *bona fide* in the best

[24] Ernest Lim, *Sustainability and Corporate Mechanisms in Asia* (CUP, 2020) at 208-217.

[25] *Brady v Brady* [1988] BCLC 20 at 40; *Greenhalgh v Arderne Cinemas Ltd* [1951] Ch 286 at 291.

[26] *Raffles Town Club Pte Ltd v Lim Eng Hock Peter* [2010] SGHC 163 at [162]; Hans Tjio et al, *Corporate Law* (Academy Publishing, 2015) at [09.045].

[27] Ibid.

interests of the company.[28] Given that the statutory duty reflects the common law duty, a breach of the statutory duty will be tantamount to a breach of the common law duty and vice versa. However, a breach of s 157(1) can attract not only civil penalties (in the form of paying damages to the company), but also criminal sanctions in the form of a fine not exceeding $5,000 or imprisonment not exceeding 12 months.

C. Application of duty in a climate risk context

As mentioned earlier, in light of the well-established and widely publicized evidence demonstrating that climate-related risks (particularly physical and transition ones) can have an adverse and material impact on the business and operations of companies, which will affect their long-term financial performance, directors are and should be required under Singapore law, in their discharge of their common law duty to act *bona fide* in the best interests of the company and the statutory duty to act honestly under s 157(1), to take into account these climate-related risks in their decision-making process, insofar as these considerations have or are likely to have a material impact on the interests of shareholders, stakeholders or the corporate entity itself.

Therefore, despite a director asserting that he has exercised his discretion in good faith in the company's best interests by not considering climate-related risks, if the court takes the view that an honest and intelligent person in the position of the director of the company in question would have taken into account those risks or would not have entered into those transactions approved by the board (had those risks been considered), the director will be in breach of the duty to act in good faith in the best interests of the company.

In other words, where climate-related risks have or are likely to have a material impact on corporate interest, and if directors deliberately or inadvertently fail to properly consider these risks -- which would include failing to give due weight to climate-related risks after considering them or failing to take actions to address the risks -- they will not meet the objective element of the *bona fide* aspect of the best interest duty.

However, there are two matters that warrant elaboration. First, what is meant by taking into account climate-related risks? Second, what if taking into account climate-related risks will conflict with short-term shareholder value?

Regarding the first issue, the board has to show how it monitors and manages the risks arising from climate change. The process of monitoring and managing should include:

(1) ensuring that adequate and appropriate resources and expertise are devoted to identifying and assessing climate-related risks, the process of which should include but are not limited to

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[28] *Townsing Henry George v Jenton Overseas Investment Pte Ltd (in liquidation)* [2007] SGCA 13 at [59].

allocating appropriate responsibilities to the relevant senior management and external experts[29];

(2) identifying and evaluating climate-related risks and the types and extent of their impact on the company with reference to different types of transactions[30], and furnishing disclosures of these risks insofar as they are material to investors; and

(3) developing and implementing climate transition action plans that are aligned with the Paris Agreement, which should include measures to address the material impacts of climate-related risks[31] such as investing in new technology, adopting low-emission energy sources, and producing low-emission products and services.

Regarding the second issue, the measures to reduce or prevent climate-related risks could involve long-term investments in, and deployment of, renewable energy and new technologies; upgrading existing equipment; or rethinking marketing and sales strategy in order to respond to shifts in, or indeed to alter, consumer behavior.[32] These measures may entail substantial expenses that could reduce short-term profitability and thus short-term shareholder value, but with the aim of improving long-term profitability and thus long-term shareholder value.

It is suggested that where incurring expenditures to reduce or prevent climate-related risks will reduce short-term shareholder value, but there is evidence, albeit inconclusive, that doing so will increase long-term shareholder value, the board will not be in breach of its duty to act *bona fide* in the company's best interests if it decides to incur such expenditures. This is because insofar as corporate interest has been equated with shareholder value, the latter has been understood not in terms of the short-term but long-term horizon. To the extent corporate interest is understood in terms of the separate and distinct interests of the company itself, the long-term value and viability of the company would require the board to take a long-term approach towards managing climate-related risks, and thus, the board will also not be in

[29] While directors can delegate and have to supervise the persons to whom they have delegated, they should acquaint themselves with a basic level of understanding of climate-related risks.

[30] For example, if directors fail to consider material physical or transition risks when they make decisions on transactions or on material capital expenditure, they will be in breach of their duties. By way of illustration, if directors in a corporate group approve a loan to a subsidiary for the purpose of pursuing fossil fuel investments, this will amount to a breach of duty.

[31] See for eg, John Colas et al, "Climate Change: Managing a New Financial Risk" (Oliver Wyman, 2019) <https://www.oliverwyman.com/content/dam/oliver-wyman/v2/publications/2019/feb/Oliver_Wyman_Climate_Change_Managing_a_New_Financial_Risk1.pdf>.

[32] GSBGEN 390: Climate Change and Capital Markets (2015) at 9 <https://law.stanford.edu/wp-content/uploads/2015/07/Climate-Change-and-Capital-Markets-FINAL-05-13-2015.pdf>.

breach of its duties if it incurs such expenditures to promote the long-term value and viability of the company.

However, if the board honestly believes that the benefit of improved long-term performance of the company arising from incurring certain expenditure to address climate-related risks is clearly outweighed by the substantial reductions in short-term profitability (because, for example, evidence of such a benefit is inconclusive or the costs of investing in new technologies significantly outweigh the benefit), the board should not be in breach of its common law and statutory duty if it decides not to incur such expenditure, provided that the board has put in place a proper and adequate system of monitoring and managing climate-related risks. This is consistent with the court's approach of not interfering with commercial decisions that are honestly made but at the same time subjecting the decision to an objective standard.

D. Conclusion

Three points are in order. First, regardless of the approach directors take towards what constitutes corporate interest—whether a shareholder primacy approach (directors should exclusively or primarily act for the benefit of shareholders), stakeholder value approach (directors should weigh and balance the interests of all stakeholders including shareholders) or a corporate entity approach (directors should promote the interests of the long-term value and viability of the company) —directors are and ought to be legally obliged to take into account risks associated with climate change insofar as these risks have a material and foreseeable impact on these interests.

Second, it does not necessarily follow from a company's compliance with the existing applicable environmental legislation or the listing rules governing sustainability reporting that the director has complied with its duty to act *bona fide* in the best interests of the company. Conversely, the fact that a company is not subject to the environmental legislation or the sustainability reporting rules does not mean that the best interest duty is inapplicable. For example, it is entirely possible for a company to have complied with the listing rules on sustainability reporting and the Carbon Pricing Act and yet be in breach of its best interest duty. This is because these rules and regulations are intended to address specific problems to achieve certain objectives. By contrast, adhering to the best interest duty is broader than mere compliance with existing environmental statutes or listing rules. It requires companies to have a proper and adequate internal system of monitoring and managing climate-related risks that are tailored to give effect to the interests of the company. Climate change is not simply an environmental compliance issue, but a business risk issue that must be managed in the best interests of the company like any other business risk.

Finally, to promote good climate risk governance and disclosure, it is necessary but insufficient that the law requires and ought to require the board to take into account climate change considerations as part of the best interest duty. Mechanisms, particularly the compensation structure, have to be put in place to incentivize directors and managers to consider climate-related risks. Their compensation scheme has to be aligned with the long-term approach needed to undertake investment in renewable energy and new technologies to reduce carbon emissions.[33]

III. COMPETENCE – DUE CARE AND DILIGENCE

A. Overview of common law duty

Directors are required to exercise reasonable care, skill and diligence. Specifically, directors are required to act with the level of care, skill and diligence that would be expected of a reasonable director in the position of the actual director—irrespective of what the actual director is capable of achieving. As the court concisely put it, "this standard is not fixed but a continuum depending on various factors such as the individual's role in the company, the type of decision being made, the size and the business of the company. However, it is important to note that, unlike the traditional approach, this standard will not be lowered to accommodate any inadequacies in the individual's knowledge or experience. The standard will however be raised if he held himself out to possess or in fact possesses some special knowledge or experience."[34]

Further, directors have a "continuing duty to acquire and maintain a sufficient knowledge and understanding of the company's business to enable them to discharge their duties."[35] And while directors can delegate the functions to management, they are required to supervise them.

B. Overview of statutory duty

The statutory equivalent of the common law duty is s 157(1) in the Companies Act which requires directors to "use reasonable diligence in the discharge of the duties of his office." The difference between the common law and statutory law however lies in the sanctions. A breach of s 157(1) attracts not only civil penalties in the form of damages, but also criminal sanction

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[33] Ibid, pg 16.

[34] *Lim Weng Kee v Public Prosecutor* [2002] SGHC 193 at [28].

[35] *Secretary of State for Trade and Industry v Baker (No. 5)* [1999] 1 BCLC 433 at 436.

in the form of a fine not exceeding $5,000 or imprisonment for a term not exceeding 12 months.[36]

It should also be noted that under s 157C, a director is permitted to rely on reports, information or advice furnished by an employee or a professional adviser, provided that the director has acted in good faith, makes proper inquiry if necessary, and has no knowledge that such reliance is unwarranted.

C. Application of duty in a climate risk context

Given that the standard of care is not fixed, but evolves with the "individual's role in the company, the type of decision being made, the size and the business of the company"[37], directors cannot ignore applicable best practices, industry norms, codes of conduct, in addition to applicable laws and regulations. There are two implications. First, directors of financial institutions, for example, will be expected to be aware of, and may be assessed in accordance with, the MAS environmental risk management guidelines as well as the TCFD recommendations mentioned above, for the purpose of determining the standard of care. Second, as for directors of non-financial institutions, even if the MAS and TCFD guidelines do not apply to them, there is a body of well-established evidence of climate-related risks to which directors cannot turn a blind eye. After all, the law imposes a minimum standard of care. Directors should at least acquaint themselves with such evidence and understand how the risks will impact on the business and operations of the company.

However, because the minimum standard of care varies with the precise functions assumed by the director as well as the size and nature of the company, the nature and extent of knowledge and the follow-up measures (particularly the internal system of monitoring and managing climate-related risks) that will be expected of directors will also vary. For example, in view of the guidelines on environmental risk management issued by MAS to banks, asset managers and insurers, the directors of these financial institutions are likely to be subject to a higher standard of care than other kinds of financial institutions. To be clear, it does not follow that a lower standard of care will be imposed on directors of non-financial institutions. After all, if the company in question belongs to the energy and resources sector, directors of these companies are arguably subject to a higher standard of care as these companies should face heightened transition risks to clean energy. Even if the company does not fall within those "high risk" sectors, if the director in question possesses special knowledge of climate-change, or if the director is a chair or member of the risk management committee, then that person will be subject to a higher standard of care. In short, the standard of care will vary according to factors such as whether the company is subject to a particular set of climate-related norms or

[36] Section 157(3) Companies Act.

[37] *Lim Weng Kee v Public Prosecutor* [2002] SGHC 193 at [28].

regulations, the sectors or industries to which the company belongs, and the type and extent of knowledge possessed by the directors and the position or responsibility assumed by them.

Finally, directors will be in breach of the duty to exercise reasonable diligence if they delegate the function of identifying and evaluating the climate-related risks and their impact to other directors or employees without adequate supervision. Directors will also be liable if they blindly rely on the advice or information provided to them[38]. They are required to exercise independent judgment[39]. Under s 157C(2) of the Companies Act, they can only rely on advice or information provided that proper inquiry is made (if warranted by the circumstances) and there is nothing to indicate that the reliance is unjustified.

D. Conclusion

To be clear, a director will not be in breach of the common law and statutory duty to exercise reasonable diligence merely because a bad decision was made in hindsight. Unlike US law which has a business judgment rule i.e. courts will not review the business decisions of directors if they have acted in good faith, with due care, and in the corporate interest[40], Singapore law does not. That said, there are dicta that courts should be slow to interfere with commercial decisions that have been honestly made.[41]

Therefore, for example, should directors invest in a new technology to mitigate a climate-related risk but bad financial consequences ensue (or decided not to invest in one after a considered cost-benefit analysis, but which subsequently turned out to be unjustified), it does not follow that they have breached the duty to exercise reasonable diligence. Rather, much will depend on the precise standard of care that will be applied to the particular director of that company in question. It will also depend on whether the director has exercised an appropriate level of supervision over the people to whom the function of monitoring and managing climate-related risks has been delegated, and whether it was justified for that director to rely on their advice or recommendation. This requires a fact and context specific exercise as discussed above.

[38] *Secretary of State for Trade and Industry v Baker (No. 5)* [1999] 1 BCLC 433 at 489.

[39] *Central Bank of Ecuador v Conticorp* [2016] 1 BCLC 26 at [45].

[40] *Aronson v Lewis*, 473 A.2d 805, 812 (1984).

[41] *Vita Health Laboratories Pte Ltd v Pang Seng Meng* [2004] 4 SLR(R) 162 at [17].

IV. DUTY OF DISCLOSURE

A. Disclosure and reporting requirements

1. Singapore Exchange Listing Rules

a. Rule 703

Under Rule 703, an issuer is subject to a continuous disclosure requirement to disclose information (1) in order avoid the establishment of a false market in its securities; or (2) that would likely have a material effect on the price or value of its securities. Regarding the first requirement, a false market may exist if information is not made available to persons in deciding whether to buy or sell securities.[42]

Regarding the second requirement, the definition of material information is vast, including "information, known to the issuer, concerning the issuer's property, assets, business, financial condition and prospects; mergers and acquisitions; and dealings with employees, suppliers and customers; material contracts or development projects, whether entered into in the ordinary course of business or otherwise … and any developments that affect materially the present or potential rights or interests of the issuer's shareholders"[43].

Given that climate change can pose material, physical, transition and even legal risks to the company, the failure to disclose material climate-related risks or the deliberate under-disclosure of such risks can amount to a breach of Rule 703 as that could lead to an establishment of a false market in its securities.

Although climate change is not explicitly mentioned in the definition of material information, the climate-related risks will affect the issuer's assets, business, and financial condition. In any event, it will and ought to be captured by "any developments that affect materially the present or potential rights or interests of the issuer's shareholders."[44] For example, if the issuer fails to take into account climate-related risks, it could produce misleading disclosures in relation to over-valuation of its assets, under-valuation of its liabilities (by under-provisioning for bad debts) or inaccurate disclosure of risk management.

A breach of Rule 703 in that a company that intentionally or recklessly fails to notify the Singapore Exchange of such information as required by the listing rules will subject the issuer

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[42] Appendix 7.1(3)(a), Corporate Disclosure Policy, SGX Listing Rule.

[43] Ibid, Appendix 7.1(4).

[44] Ibid.

to a fine.[45] As a result, the directors of the issuer will be in breach of their common law and statutory duty to exercise reasonable diligence.

b. Rules 711A, 711B

Under Rule 711A, companies are required to furnish an annual sustainability report, the contents of which according to Rule 711B include but are not limited to material environmental, social and governance factors; policies, practices and performance; targets; sustainability reporting framework; and board statement.

Should the company be unable or unwilling to make the requisite disclosure, they have to provide an explanation, given that the sustainability report operates on a "comply or explain" basis. While the listing rules do not impose any sanctions for inadequate disclosure in the sustainability report, the company can be liable under the common law for fraudulent or negligent misrepresentations (provided that the elements of causation and losses are also proven). If the company were to be held liable, directors may be in breach of the duty to exercise reasonable diligence under the statute and common law.

2. Banking Act

In order to enhance market discipline, the MAS may require banks to disclose to the public any information relating to their operations and activities which includes the risk profile and risk management process of the banks.[46] One cannot rule out the possibility that should MAS require banks to disclose information pursuant to its environmental risk management guidelines, a failure to do so, or where the bank knowingly or recklessly provides any false or misleading information, the bank could be fined. In addition, if the directors have not used reasonable care to ensure that the information is not false or misleading in any material aspects, they could be fined and/or imprisoned.[47]

V. ESTABLISHING LIABILITY

[45] Sections 203 and 204 Securities and Futures Act (Cap 289).

[46] Sections 10B(1) and 10B(2) Banking Act (Cap 19) (see also s 26(1)).

[47] Section 66(2) Banking Act.

A. Evidentiary requirements

At the outset, one of the evidentiary obstacles in establishing liability lies in detecting and investigating actual and potential wrongdoing. If the board does not sue the delinquent director, the burden is on investors to do so. However, unless investors have access to evidence demonstrating actual or potential wrongdoing, they will not be successful in bringing their claims. One tool available to the claimant-members is that they can exercise their statutory right to inspect the minute books of board meetings and general meeting of shareholders.[48] They have to pay S$1 for every page of the minutes that they have requested.[49] If the company fails to supply the requested information, the company and its directors may be fined.[50]

1. Common law

Under the common law, a breach of the directors' duty to exercise reasonable diligence (a non-fiduciary duty) will result in common law damages whereas a breach of the duty to act *bona fide* in the company's best interests (a fiduciary duty) will result in equitable compensation.[51]

In the case of common law damages, the claimant has to prove but for causation, and the elements of foreseeability and remoteness will apply. Thus in order for the claimant to succeed in a claim that the director has breached the common law duty to exercise reasonable diligence, not only does the claimant have to establish that a duty of care was owed to the company in respect of the kind of loss which the company has suffered, but also that the loss claimed is attributable to the breach of duty relied on.[52]

But in the case of equitable compensation, the claimant does not need to prove but for causation, and the elements of foreseeability and remoteness do not apply. Instead, the defendant fiduciary bears the legal burden of proving that the loss would have been sustained by the principal even if the fiduciary had not breached their fiduciary duty.[53]

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[48] Section 189(2) Companies Act.

[49] Ibid.

[50] Ibid, section 189(3).

[51] Hans Tjio et al, *Corporate Law* (Academy Publishing, 2015) at [09.105].

[52] See eg, *Re Continental Assurance Co of London plc* [2007] 2 BCLC 287 at [378]-[380], [405]; *Madoff Securities International Ltd v Raven* [2013] EWHC 3147 at [294].

[53] *Sim Poh Ping v Winsta Holdings Pte Ltd* [2020] SGCA 35.

Thus, it should be arguably easier to make a case that under the common law, directors have breached their fiduciary duty to act *bona fide* in the company's best interests when they failed to take into account climate-related risks than to argue that directors have breached their non-fiduciary duty to exercise reasonable diligence.

2. Statutory law

As examined earlier, the statutory equivalent of the duty to act *bona fide* in the best interests of the company and the duty to exercise reasonable diligence can be found in s 157(1) of the Companies Act. Given that s 157(1) attracts criminal sanctions, the public prosecutor has the burden of proving beyond a reasonable doubt that the offence has been made out. Given the seriousness of the offence under s 157(1), there are few reported cases of directors who have been convicted for breaching the duty to exercise reasonable diligence.

The Companies Act is not the only legislation that subjects directors to criminal liability as other environmental legislation do so. For example, under s 68(2) of the Carbon Pricing Act, where a company has committed an offence under the statute, an officer of the company or an individual in the company's management and in a position to influence the conduct of the company in relation to the offence, and who (i) consented or connived, or conspired with others to commit the offence; or (ii) is knowingly concerned in or is party to the commission of the offence; or (iii) knew or ought to have known that the offence by the company would be committed and failed to take all reasonable steps to prevent the offence, shall be guilty of the same offence as the company.

B. Possible defenses[54]

Section 391 of the Companies Act provides that if a director has been liable for negligence, default, breach of duty or breach of trust, but has acted honestly and reasonably, and having regard to all the circumstances of the case, that person ought fairly to be excused, the court may relieve the director either wholly or partly from liability.

In order for relief under s 391 to be obtained, two elements must be proven by the director: first, the director has acted honestly; and second, the director has acted reasonably.[55] Then the court has to decide whether the director ought fairly to be excused, having regard to

[54] Note that the business judgment rule is not a recognized statutory defence under Singapore law. But courts have stated *obita* that they would be slow to interfere in commercial decisions that are honestly made: *Vita Health Laboratories Pte Ltd v Pang Seng Meng* [2004] 4 SLR(R) 162 at [17].

[55] *JSI Shipping (S) Pte Ltd v Teofoongwonglcloong (a firm)* [2007] SGCA 40, [2007] 4 SLR(R) 460; *Long Say Ting Daniel v Merukh Nunik Elizabeth* [2014] 1 SLR 1428.

matters including but not limited to the position held by the director, and the seriousness of the breach and the consequences.

However, because s 391 requires that the director has acted honestly and reasonably, if a director has breached the duty to act *bona fide* in the best interests of the company, he will not be permitted to rely on s 391. This is because he would have flouted the subjective element of the duty (which requires that he acted honestly) and/or the objective element (which requires that the decision is one that an honest and intelligent person in the position of the director would have made).

Finally, s 391 does not apply to criminal proceedings.[56] Thus, judicial relief from liability only applies if a person is liable for breaches under the common law. Therefore, even if a director is relieved from liability for breaching the common law duty to exercise reasonable diligence under s 391, the court has no discretion to relieve the director from the penal consequences of being convicted under s 157(3)(b).

C. Personal liability and availability of D&O insurance

Section 172 of the Companies Act provides that any provision in the corporate constitution or in an agreement between the company and directors that (1) exempts directors from any liability or (2) indemnifies directors against any liability, will be void, except for insurance purchased by the company for the directors against such liability.[57] The statute further clarifies that no indemnification is permitted in criminal proceedings or where the director is being sued by the company. Thus, should directors be convicted for breach of the duty to act honestly and with reasonable diligence under s 157(1), no indemnification is allowed.

VI. ENFORCEMENT

A. Derivative action

If the board decides not to sue the delinquent director for breach of duties, or if the general meeting (which can include the delinquent director) ratifies a breach of common law duty by

[56] *Re IDEAGLOBAL.COM Ltd* [2000] 1 SLR(R) 804.

[57] The scope of the insurance coverage will exclude fraud.

the director[58], a minority shareholder can bring derivative action on behalf of the company against the delinquent director.

Common law and statutory derivative actions are available under Singapore law in order to address breaches of duties committed by directors against the company. Common law derivative action is available to companies incorporated in Singapore and overseas. But the statutory derivative action is only available to companies incorporated in Singapore.[59]

There are drawbacks to the common law derivative action. In order for this action to succeed, the claimant has to prove that the wrongdoer has committed a fraud on the minority.[60] This arguably requires three elements to be proven:

- the wrongdoer has obtained some sort of benefit;
- the benefit was obtained at the company's expense; and
- the wrongdoer used his controlling power to prevent an action from being brought against him by the company.[61]

Thus, if the delinquent director has breached the duty to exercise reasonable diligence but has not obtained any benefit, the first element will not be satisfied. This will pose an obstacle where directors have been negligent because they have failed to monitor and manage climate-related risks that have a material and foreseeable impact on the company's business, but they have not obtained any benefit. By contrast, in a statutory derivative action, there is no requirement for the wrongdoer to have gained a benefit.

Another drawback to the common law derivative action is that this action may not be permitted by the court if the action is opposed by a majority of independent shareholders or independent directors.[62] By contrast, there is no such obstacle in a statutory derivative action (unless the court interprets the opposition by the independent directors or independent shareholders as evidence of the derivative action not *prima facie* in the interests of the company).

In view of the drawbacks to the common law derivative action, it would be preferable for minority shareholders in Singapore incorporated companies to resort to the statutory derivative action under s 216A of the Companies Act.

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[58] Note that a breach of a statutory duty cannot be ratified.

[59] See section 216(A)(1) read together with section 4(1) regarding the definition of "company".

[60] *Sinwa SS (HK) Co Ltd v Morten Innhaug* [2010] 4 SLR 1.

[61] Tan Cheng Han, *Walter Woon on Company Law* (Sweet & Maxwell, Revised 3rd edn, 2009) at 372; Margaret Chew, *Minority Shareholders' Rights And Remedies* (Lexis Nexis, 3rd ed, 2017).

[62] *Smith v Croft (No 2)* [1988] Ch 14; *Ting Sing Ning v Ting Chek Swee* [2008] 1 SLR 197.

Under s 216A, the complainant must be a member of the company, the Minister of Finance, or any other person the court deems proper. The complainant is required to satisfy three elements:

- first, he must give 14 days' notice to the directors of the company that he will commence the action if they decide not to bring an action;
- second, he must prove that he is acting in good faith;
- and finally, he has to demonstrate that the action appears to be *prima facie* in the interests of the company.

In determining whether the last requirement is satisfied, the court will consider first, the costs and benefits of the derivative action; second, the likelihood of success of any action; and finally, the availability of alternative measures.[63]

The most important disadvantage of the derivative action (both common law and statutory) is that any damages that the court will award will go to the company and not to the shareholder who brought the lawsuit. This, coupled with the prohibition of contingency fee arrangements and class action suits in Singapore, often disincentivizes derivative actions from being brought.

That said, even if minority institutional or retail shareholders are reluctant to bring derivative law suits for the above reasons, one cannot rule out the possibility that environmental NGOs will buy shares in the company in order to bring such an action (provided that the three elements under s 216A are satisfied). This is one of the strategies that has been adopted with success in other jurisdictions, and companies in Singapore must be prepared for this possibility.[64]

B. Oppression

Generally, breaches of directors' duties amount to wrongs done to the company and thus a derivative action under s 216A is the appropriate course of action. But for wrongs committed personally against the minority shareholder, the claimant, who is required to be a member of the company, should resort to oppression under s 216 of the Companies Act which only applies to Singapore incorporated companies.[65]

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[63] *Wong Lee Vui Willie v Li Qingyun* [2016] 1 SLR 696.

[64] "Major Court win shows power of corporate law to fight climate change" ClientEarth (1 August 2019) <https://www.clientearth.org/latest/latest-updates/news/major-court-win-shows-power-of-corporate-law-to-fight-climate-change/>; "Green Investors Are Embracing Litigation: Some Are Winning" Economist (21 November 2020).

[65] *Lim Chee Twang v Chan Shuk Kuen Helina* [2010] 2 SLR 209.

However, a breach of director's duty can form the basis for an oppression claim under s 216 of the Companies Act provided that the court is satisfied that the claimant is not abusing the process by invoking s 216.[66] To determine whether there has been an abuse of process, the court has devised a two-part test.[67]

The first part of the test concerning the injury comprises two questions:

1) what is the real injury that the plaintiff seeks to vindicate?
2) is that injury distinct from the injury to the company and does it amount to commercial unfairness against the plaintiff?

The second part of the test relates to remedies and consists of two questions:

1) what is the essential remedy that is being sought and is it a remedy that meaningfully vindicates the real injury that the plaintiff has suffered?
2) is it a remedy that can only be obtained under s 216?

If the answer is yes to both sets of questions, then the oppression claim will succeed. But if the essential remedy sought is a remedy for the company (such as a restitutionary order in favor of the company), the presumptively appropriate remedy would be the statutory derivative action under s 216A. That said, if the essential remedy sought is, for example, a share buyout, the claimant can also seek remedies in favor of the company such as restitutionary orders given that the latter remedy will impact on the essential remedy sought.[68]

The court also remarked *obita* that the application of these two sets of questions will generally exclude recourse to oppression actions in cases involving publicly or widely-held companies because either the essential remedy sought or the real injury complained of will quite likely not bring the case within s 216.[69] Another dictum is that a breach of the duty to exercise reasonable diligence will not be evidence of oppression under s 216 unless the breach was sufficiently serious to amount to commercial unfairness.[70]

Despite these dicta, it is arguable that a shareholder of a company can bring an oppression suit by alleging that a breach of an agreement between the company and shareholders amounts to commercial unfairness; this is because commercial unfairness can arise from breaches of the corporate constitution, shareholders' agreement, or applicable rules and

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[66] *Ho Yew Kong v Sakae Holdings Ltd* [2018] SGCA 33.

[67] Ibid at [116].

[68] Ibid at [119].

[69] Ibid at [121].

[70] Ibid at [152].

regulations.[71] Thus, for example, should a listed company breach its agreement (whether written or implied) with its shareholders that it will comply with the listing rules, thereby causing losses to the shareholders, the court can allow a shareholder's action to succeed. This was the case in an important Hong Kong decision on unfair prejudice (which is similar to Singapore's oppression action).[72]

Therefore, by way of illustration in the context of climate-related risks, if a company listed on the Singapore Exchange breaches its disclosure obligations under the listing rules by not disclosing a material climate-related risk, this may amount to a breach of an implied agreement between the company and shareholders that the company will comply with the listing rules, thereby arguably warranting an oppression action under s 216.

C. Remedies

The remedies that the court can award pursuant to a statutory derivative action is not spelled out in the Companies Act. But it is well-established that the court can award the common law remedy of compensatory damages for breach of the directors' common law and statutory duty to exercise reasonable diligence. As for a breach of the fiduciary duty to act in good faith in the best interests of the company, the court can award equitable compensation. Insofar as the director has received unauthorized benefits in breach of the no-profit rule (which is outside the scope of this paper), the director will be required to disgorge the profits.

The remedies that the court can award for oppression are stated in s 216(2) of the Companies Act; these include:

- directing or prohibiting any act or cancelling or varying any transaction or resolution;
- regulating the company's affairs;
- authorizing civil proceedings to be brought in the company's name;
- ordering the claimant's shares to be bought out; and
- ordering the company to be wound up.

VII. CONCLUSION

[71] *Over & Over Ltd v Bonvest Holdings Ltd* [2010] SGCA 7.

[72] *Luck Continent Ltd v Cheng Chee Tock Theodore* [2012] HKEC 567.

In light of the extensive and well-established evidence that climate-related risks pose to the interests of the company, in view of the government's recognition that such risks pose to Singapore's economy, and because of the increasing soft law and hard law measures taken by the Singapore authorities to address climate-related risks, a reasonable director is and ought to be legally required to take into account climate-related risks in its discharge of duties to the company, failing which the director may be held civilly and criminally liable, not to mention the adverse reputational repercussions on that director and the company.

Such legal requirements are manifested not only in the common law and statutory law governing the duties of directors to act *bona fide* in the best interests of the company and to exercise reasonable diligence, but also in the disclosure obligations imposed by the listing rules and other legislation.

Should directors be in breach of their duties under the common law or statute, they may be subject to criminal sanctions or regulatory penalties, and may be dismissed or sued by the board. Minority shareholders can also bring civil proceedings against them. Finally, one cannot rule out the possibility that the company may be sued by other interested parties (who are non-shareholders).[73]

[73] See for eg, Asian Development Bank, Climate Change, "Coming Soon to a Court Near You: Climate Litigation in Asia and the Pacific and Beyond" (Dec 2020).

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