PENGURUSAN DANAHARTA NASIONAL BERHAD - A CASE FOR IMPOSING FIDUCIARY DUTIES ON THE SPECIAL ADMINISTRATOR

1. Introduction

As a result of the recenteconomic collapse - the Malaysian government has established two entities to help revitalise local financial institutions. One is Danamodal with the specific objective to recapitalise troubled financial institutions. The other entity is Pengurusan Danaharta Nasional Berhad ("Danaharta") to acquire selected non-performing loans of these financial institutions. In this paper I will focus on Danaharta.

Danaharta is incorporated pursuant to Pengurusan Danaharta Nasional Berhad Act 1998[1] ("the Act").

The objectives of the Act are to:[2]

(a) assist financial institutions by removing impaired assets;
(b) assist the business sector by dealing expeditiously with financially distressed enterprises; and
(c) promote the revitalisation of the nation's economy.

These objectives will be met by the establishment of Danaharta which is equipped with the powers to acquire, manage, finance and dispose assets and liabilities. Danaharta is also empowered to appoint a Special Administrator to administer and manage the companies[3] whose assets and liabilities have been acquired by it.[4]

The appointment of the Special Administrator as provided by the Act is can be compared to the appointment of receivers and/or managers,

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[1]Act 587.

[2]The Act, Preamble, paragraph 1.

[3]Defined in the Act as 'affected person' - section 21.

[4]The Act, part VI.

liquidators, administrators[5] or judicial managers,[6] as a receiver and/or manager is appointed by creditors pursuant to a debenture, a liquidator is appointed by the court[7] and an administrator and judicial manager is appointed by the court upon an application made by the company or a creditor. In Danaharta's case, the appointment of the Special Administrator can only be made by Danaharta with the approval of the Oversight Committee.[8] The members of the Oversight Committee will be appointed by the Minister of Finance and shall consist of the representatives of the Ministry of Finance, the Central Bank and the Securities Commission.[9]

The prerequisite for the appointment of the Special Administrator is that Danaharta is of the view that the company is unable or likely to become unable to pay its debts or is unable or likely to become unable to satisfy its obligations to its' creditors.[10]

2. Functions of the Special Administrator

The objective of appointing a Special Administrator is to fulfill a public interest, or either to ensure the continued survival of the company as a going concern, or to achieve a more advantageous realisation of the company's assets compared to winding up.[11]

3. Powers of the Special Administrator

The Special Administrator shall be entitled to exercise all the functions of the board of the company.[12] Once appointed, none of the officers of the company, including the directors, shall be allowed to function and

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[5]Pursuant to the United Kingdom Insolvency Act 1986.

[6]Pursuant to the Companies Act of Singapore (Cap. 50).

[7]Or the company or creditors in the case of a voluntary winding up.

[8]The Act, sections 23 and 24.

[9]The Act, section 22(2).

[10]Section 24.

[11]The Act, section 25.

[12]The Act, section 33(2).

exercise their duties as officers of the company without written consent of the Special Administrator.[13] In addition, the Special Administrator shall have certain statutory powers as listed in the Second Schedule of the Act.[14]

In effect, once a Special Administrator has been appointed by Danaharta, the management of the company will be in the hands of the Special Administrator.

4. Duties of the Special Administrator

4.1 To Whom Duties are Owed and Nature of Duties

The general duties of the Special Administrator are provided in section 31 of the Act, which provides that the Special Administrator shall take control or custody of all the assets of the company and shall manage the assets and affairs of the company. Section 14 of the Act provides for the vesting of the assets in Danaharta.

However, the Act is silent as to whether the Special Administrator owes a duty to the company, it's other creditors, or shareholders of the company. This may be compared with the position of receivers and/or managers, liquidators, administrators and judicial managers. A receiver and/or manager has a primary duty to the debenture holders who appointed him.[15] A liquidator owes his duties to the company, the creditors and contributories.[16] An administrator and judicial manager owes his duties to both creditors and members of the company.[17]

As for the nature of the duties, a receiver and/or manager has fiduciary duties.[18] A liquidator similarly has fiduciary duties.[19] An

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[13]The Act, section 33(1).

[14]The Act, section 30.

[15]See, example, *Re B Johnson & Co (Builders) Ltd* [1955] 1 Ch 634. But the receiver also has duties to the company: see Woon, *Company Law* (1997), at page 501.

[16]B.H. McPherson J., *The Law of Company Liquidation* (1987), at page 214, cited with approval by *Re G.K. Pty Ltd; Ex Part D.C.T.* (1983) 7 A.C.L.R. 804.

[17]U.K. Insolvency Act 1986, section 27; Companies Act of Singapore, section 227R.

[18]See *Roman Tomasic and Stephen Bottomley,* Corporations Law in Australia (1995), at page 879.

[19]B.H. McPherson J., The Law of Company Liquidation (1987), at page 214.

administrator and judicial manager has a duty to act fairly to both creditors and members of the company.[20]

4.2 Can a Duty be Formulated by the Courts?

In the absence of a specific duty imposed on to the Special Administrator, can a duty be formulated by the courts?

It is to my mind inconceivable that the Special Administrator does not owe any duty to the shareholders and creditors of the company, since the Special Administrator will have control over the management of the company. Other company controllers, including directors and controlling shareholders, have fiduciary duties, in addition to duties to act fairly to the shareholders and debenture holders, as provided by section 181 of the Companies Act 1965. Administrators and judicial managers have similar duties to creditors and members of the company, as provided by the respective Insolvency Act and Companies Act of Singapore. This begs the question: why the omission?[21] It should not be forgotten that on the appointment of the Special Administrator, a moratorium will be forced on the creditors from recovering their debts or realising their securities.[22] Furthermore, the Special Administrator, in managing the assets of the company, shall act in accordance with the directions given by Danaharta.[23]

4.2.1 Duties to the Company

Can there be an argument that the Special Administrator owes a duty to the company? It may be possible. For support of this proposition

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[20]U.K. Insolvency Act 1986, section 27; Companies Act of Singapore, section 227R. Hence, a creditor or member of the company may apply to court for an order if the administrator or judicial manager has acted in a manner which is unfairly prejudicial to the interests of its creditors or members.

[21]It should also be noted that the Act works in ways similar to those of the Insolvency Act of U.K. and the Companies Act of Singapore. Is this omission deliberate?

[22]The Act, section 41.

[23]The Act, section 31(2). This is prior to the approval of the proposal to be given under section 46 of the Act.

I refer to the Canadian Supreme Court decision in *Canadian Aero Services Ltd v O'Malley*[24] where two senior officers of a company were held to be directors as their positions have the characteristics of the position of directors.

This view is correct and consistent with the definition of "director" as provided in section 4(1) of the Companies Act 1965, which "includes any person occupying the position of director of a corporation by whatever name called ...", that is, de facto director.[25]

In a more recent case, *Yukong Line Ltd of Korea v Rendsburg Investments Corp of Liberia and others (No 2)*,[26] Toulson J., equates the position of a person having the management of a company with the position of a director.[27]

One can therefore argue that the Special Administrator has fiduciary duties to the company. The Special Administrator will also be bound to act fairly to members and debenture holders of the company pursuant to section 181 of the Companies Act 1965.

4.2.2 Duties to the Creditors Generally

What about the creditors? As I had mentioned earlier, a liquidator, receiver, administrator and judicial manager all have certain duties to creditors of the company.[28]

I have also argued that a Special Administrator owes fiduciary duties to the company (by virtue of the characteristics of their office), and it is on this basis that I shall proceed.

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[24](1973) 40 DLR 3d 371.

[25]It is unfortunate, however, that in more recent cases (e.g. *Secretary of State for Trade and Industry v Tjolle* [1998] 1 BCLC 333, *Re Hydrodam (Corby) Ltd* [1994] 2 BCLC 180), the courts are more preoccupied with the question whether the "director" is holding out or is held out by the company as a director so as to make the question whether a Special Administrator is a director relevant.

[26][1998] 2 BCLC 485.

[27]*Ibid*, at page 99.

[28]Although a receiver and manager owes a primary duty to the debenture holder.

There has yet to be formulated a comprehensive and consistent principle as to the duties of directors to creditors although it has been 23 years since Mason J. ruled that:

> ... the directors of a company in discharging their duty to the company must take account of the interests of its shareholders and its creditors.[29]

Although it is now settled law that directors owe certain duties to the company's creditors,[30] the law is not certain as to the nature of the duties that can be said to arise.

In *Walker v Wimborne*,[31] the Australian High Court indicated that directors in discharging their duties to the company have to take into account the interests of creditors, as well as the shareholders. It would appear that interests of creditors are merely a subset of a wider duty owed to the company generally. This view was echoed in New Zealand[32] and England.[33]

On the other hand, there are authorities suggesting that the duties are owed to the creditors. In *Winkworth v Edward Baron Development Co Ltd*,[34] Lord Templeman of the House of Lords ruled that directors owe fiduciary duties directly to creditors.[35]

The issue of whether directors owe a duty to creditors as a subset of a more general duty owed to the company or the duties are owed directly to the creditors is important to determine whether the creditors

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[29]*Walker v Wimborne and Others* (1976) 137 C.L.R. 1.

[30]As evidenced by subsequent Australian, New Zealand and English cases affirming Mason J.'s statement: see, e.g. *Kinsela v Russell Kinsela Pty Ltd* (1986) 4 NSWLR 722; *Jeffree v National Companies and Securities Commission* (1989) 7 A.C.L.C. 556; *Nicholson v. Permakraft (N.Z.) Ltd* [1985] 1 N.Z.L.R. 242; *Winkworth v Edward Baron Development Co Ltd* [1987] 1 All ER 114; *West Mercia Safetywear Ltd (in liq) v Dodd* [1998] BCLC 250; *Facia Footwear Ltd v Hinchliffe* [1998] 1 BCLC 218; *Yukong Line Ltd of Korea v Rendsburg Investments Corp of Liberia and others (No 2)* [1998] 2 BCLC 485.

[31](1976) 137 C.L.R.

[32]See *Nicholson v Permakraft* [1985] 1 NZLR 242.

[33]See *Lornho v Shell Petroleum* [1980] 1 WLR 627.

[34][1987] 1 All ER 114.

[35]See also *Hooker Investments Pty Ltd v Email Ltd* (1986) 10 ACLR 443.

may take an action against the directors for a breach of the duty, and whether the shareholders can ratify a breach of duty.[36]

The law is also not certain as to the time the duties can be said to arise. In *Ring v Sutton*,[37] Hope J.A., citing Mason J. in *Walker v Wimborne and Others*,[38] held that a duty to creditors arises even when the company is not insolvent. However, in *Kinsela v Russell Kinsela Pty Ltd*,[39] Street CJ thought that only when the company is insolvent the interests of creditors intrude.[40]

Although the law is by no means settled, it is now a well established principle of law that directors must have agreed to the creditors of the company, and invariably so when the company is insolvent.[41] Therefore, the same can be said for the Special Administrator.

4.2.3 Duties to Danaharta as an Individual Creditor

Can the Special Administrator be said to owe a primary duty to Danaharta as their appointor?

The case of *Yukong Line Ltd of Korea v Rendsburg Investments Corp of Liberia*[42] offers some guidance in this issue. One of the issues here was whether a creditor may sue a controlling shareholder who controls the management of the company for breach of fiduciary duty. Toulson J. said:

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[36]For a discussion on this issue, see Sarah Worthington, 'Directors' Duties, Creditors' Rights and Shareholder Intervention' (1991) 18 M.U.L.R. 121. For some conceptual discussion, see L.S. Sealy, 'Directors' "Wider" Responsibilities – Problems Conceptual, Practical and Procedural' (1987) 13 Mon LR 164.

[37](1980) 5 A.C.L.R. 546.

[38](1976) 137 C.L.R 1.

[39](1986) 4 ACLC 215.

[40]A similar view was expressed by Dillon LJ in *West Mercia Safetywear Ltd v Dodd* [1988] BCLC 250.

[41]See Vanessa Finch, 'Creditor Interests and Directors' Obligations' in Saleem Sheikh and William Rees (eds), *Corporate Governance & Corporate Control*, (1995), at pages 118-119. See also Philip Goldberg, 'IALS Company Law Lecture - Shareholders v Stakeholders: The Bogus Argument' (1998) 19(2) *Company Lawyer* 34.

[42][1998] 4 All ER 82.

> In my view [the controlling shareholder who is in a fiduciary position] does not owe a direct fiduciary duty towards an individual creditor, nor is an individual creditor entitled to sue for breach of the fiduciary duty owed by the director to the company.[43]

Using this case as my guidance, it would appear that the Special Administrator, although appointed by Danaharta, must act in the interests of the creditors in general and not to Danaharta as their appointor.[44]

5. Danaharta as Shadow Director

Section 31(2) of the Act provides that '[t]he Special Administrator shall manage the asset and affairs of the affected person ... in accordance with any directions given by [Danaharta]'. As the Special Administrator is a 'de facto director', that would make Danaharta a 'shadow director', within the definition of 'director' as provided by section 4(1) of the Companies Act 1965. Therefore Danaharta too has fiduciary duties to the company and must have regard to the interests of the creditors and shareholders, together with a duty to act fairly to the members and debenture holders of the company pursuant to section 181 of the Companies Act 1965.

6. The Finding of Fiduciary Duty Through "Equity Jurisprudence"

Apart from arguing that the Special Administrator owes fiduciary duties to the company as a 'shadow director', it may also be possible to argue that the fiduciary duties may also arise as a result of 'equity jurisprudence', to borrow the term used by Gopal Sri Ram JCA in *Tengku Abdullah ibni Sultan Abu Bakar v Mohd Latiff bin Shah Mohd.*[45] In this case, one of the issues was whether promoters of a proprietary

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[43]*Ibid*, page 99.

[44]For a further discussion on directors' duties to individual, existing, future or classes of creditors, see Vanessa Finch, 'Creditor Interests and Directors' Obligations' in Saleem Sheikh and William Rees (eds), *Corporate Governance & Corporate Control*, (1995), at pages 115-117.

[45][1996] 2 AMR 2633, pages 2672-2673.

club were fiduciaries. The Court of Appeal answered the question in the affirmative. In reaching his decision, Gopal Sri Ram JCA quoted a number of cases, including *Hospital Products Ltd v United States Surgical Corporation*.[46] The learned judge also quoted general characteristics of fiduciary relationships proposed by Wilson J. in *Frame v Smith*.[47] These characteristics are:

(1) the fiduciary has scope for the exercise of some discretion or power:
(2) The fiduciary can unilaterally exercise that power or discretion so as to affect the beneficiary's legal or practical interests; and
(3) The beneficiary is peculiarly vulnerable to or at the mercy of the fiduciary holding the discretion or power.

Based on these characteristics, his Lordship concluded that the promoters were fiduciaries.

It is certainly arguable that these characteristics fits the Special Administrator. The Special Administrator has scope for the exercise of some discretion or power. This is provided by the Act, as discussed earlier. These powers may be used to affect the creditors' interests in the company and the creditors are vulnerable to the Special Administrator. This vulnerability may be as a result of the moratorium imposed on the creditors in relation to the company's debts.[48] In addition, unsecured creditors will be particularly vulnerable as they are not even allowed to vote in relation to the proposal to be submitted by the Special Administrator pursuant to section 46 of the Act. Hence, fiduciary duties by way of 'equity jurisprudence'.

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[46](1986) 156 CLR 41.

[47](1987) 42 DLR (4th) 81. See *Tengku Abdullah ibni Sultan Abu Bakar v Mohd Latiff bin Shah Mohd*, *supra*, at page 2671.

[48]The Act, section 41.

7. Why is it Necessary to Impose a Duty to the Special Administrator?

This duty is important as:

(a) the rights of members will be suspended pending the approval of the proposal by the secured creditors pursuant to section 46 of the Act;
(b) the rights of creditors against the debtor company will be frozen[49] pending the approval of a proposal to be submitted by the Special Administrator to Danaharta[50] and the creditors; and[51]
(c) only the secured creditors will have a right to attend and vote at the creditors meeting.[52] The unsecured creditors and the secured creditors who vote against the Special Administrator's proposal will have no avenue to forward their complaints, if they had been neglected or unfairly treated.

8. Conclusion

The omission by our lawmakers to spell out the duties of the Special Administrator will result in an unnecessary burden on our courts to formulate some sort of duty. Nevertheless, I have little doubt that, if given the opportunity, the courts will make the necessary comparison between the position of the Special Administrator and that of directors, liquidators, administrator and judicial manager, and hold that the Special

[49]The Act, section 41.

[50]The Act, section 45.

[51]The Act, section 46.

[52]*Ibid.*

Administrator (and Danaharta, for that matter) shall act in the best interests of the company and its creditors.

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LAND CONTRACTS AND ESTOPPEL: RELIEF WHERE NONE SHOULD BE GRANTED?

The Common Law and the Sale and Purchase Agreement [SPA]

In Hong Kong, the common law rule that time is of the essence in the performance of contractual time stipulations applies automatically to contracts for the sale and purchase of land unless there is an express term against the essentiality of time: *Luxebond Investment Ltd v Super Asian Investment Ltd*[1] and *Chong Kai Tai v Lee Gee Kee*.[2] The equitable rule, found in section 11 of the *Law Amendment and Reform (Consolidation) Ordinance*[3] reverses the common law rule unless the parties provide to the contrary and applies automatically to most other contracts. Essentiality of time in the SPA relates not only to a specific day but also to a specific time on that day; where the date only is essential, the 'midnight rule' applies: *Camberra Investment Ltd v Chan Wai-tak*.[4]

The innocent party can treat the breach of an express time stipulation either as a breach of a condition, or as an offer of repudiation. Breach of a condition results either in specific performance and perhaps damages for the delay, or in damages on the termination of the contract. Acceptance of an offer of repudiation by the innocent party terminates the contract, enabling the offeree to seek compensation. The choice of accepting or rejecting the offer may well depend on the state of the market, and the identity of the offeror. More usually the offeror is the purchaser, and the vendor accepts the offer. Unless the contract provides

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[1][1998] 2 HKC 108.

[2][1997] 1 HKC 359.

[3]Cap 23.

[4][1989] 1 HKLR 568: Law Society Circular 15/89.