Tang Yoke Kheng (trading as Niklex Supply Co) v Lek Benedict and Others (No 2) [2004] SGHC 215

Case Number : Suit 864/2003

Decision Date : 27 September 2004

Tribunal/Court : High Court

Coram : Andrew Ang JC

Counsel Name(s) : P Suppiah and Elengovan Krishnan (P Suppiah and Co) for plaintiff; Daniel John and Lim Fung Peen (John Tan and Chan) for first and second defendants; Daryll Ng and Nicole Tan (Haridass Ho and Partners) for third defendant

Parties : Tang Yoke Kheng (trading as Niklex Supply Co) — Lek Benedict; Lim Wee Chuan; Tan Te Teck Gregory

Companies – Winding up – First and second defendants directors of company -First and second defendants causing company to purchase goods on running account from plaintiff then transferring such goods to other related companies – Plaintiff alleging first and second defendants causing company to continue trading even though company insolvent – Whether first and second defendants knowingly parties to carrying on of business of company with intent to defraud creditors – Whether first and second defendants liable for company's debts – Section 340(1) Companies Act (Cap 50, 1994 Rev Ed)

Tort – Conspiracy – Whether third defendant conspiring with first and second defendants in alleged wrongdoings

27 September 2004 Judgment reserved.

Andrew Ang JC:

1 The plaintiff, trading as Niklex Supply Co ("Niklex"), is a creditor of Amrae Benchuan Trading Pte Ltd ("the Company"), now in liquidation, of which the first and second defendants were at all material times the directors and shareholders. The third defendant was an employee of the Company.

2 The gravamen of the claim by the plaintiff is that the business of the Company had been carried on with intent to defraud creditors of the Company (in particular the plaintiff or Niklex) in breach of s 340(1) of the Companies Act (Cap 50, 1994 Rev Ed) ("the Act").

3 Adopting a "blunderbuss approach" in the Re-Amended Statement of Claim, the plaintiff also alleged breaches of ss 157 and 339(3) of the Act and sought to invoke s 409A of the Act. However, the plaintiff's counsel, Mr P Suppiah did not, at any stage of the trial, pursue them. That is just as well; no civil suit can be commenced in respect of a breach of s 339(3) until there has been a conviction for the offence. As for s 157, it merely imposes upon a director a duty at all times to act honestly and to use due diligence in the discharge of his duties. By itself, it confers no rights on a creditor. Although the provisions of s 409A could, in an appropriate case where the court has power under the section to grant an injunction, be invoked to found a claim for damages in respect of a breach of s 157 (or indeed of any other provisions of the Act), the remedy is not available to the plaintiff in this case; the interlocutory injunction taken out by the plaintiff has been discharged by the order of Lai Kew Chai J and this has been upheld despite the plaintiff's appeal to the Court of Appeal.

4 As set out in the Re-Amended Statement of Claim, the plaintiff's numerous allegations against the first and second defendants, with a view to proving intent on their part to defraud the Company's

creditors, included the following:

(a) Although the Company was insolvent from 1999 onwards, the first and second defendants caused the Company to continue trading;

(b) The first and second defendants paid salaries, bonuses, travelling expenses to themselves and to the third defendant in 2000 and 2001;

(c) The first and second defendants wrongfully caused the Company to grant loans to themselves and to the third defendant in 2000 and 2001, which loans were never repaid;

(d) In order to dissipate the Company's assets, the first and second defendants wrongfully caused the Company to:

(i) pay $32,067.84 to Axum Marketing Pte Ltd ("Axum") of which the defendants were shareholders and directors;

(ii) spend $283,769.31 on advertising and promotion in 2002 when the Company was insolvent;

(iii) pay $100,000 as reimbursement of petty cash; and

(iv) pay Concept Gifts Pte Ltd ("Concept Gifts") $125,000;

(e) The first and second defendants wrongfully dissipated the Company's assets in order to put them out of the reach of Niklex by transferring them to allegedly related companies, *ie*, Amrae Benchuan Sdn Bhd ("Amrae Sdn Bhd"), Amrae Benchuan International Pte Ltd ("Amrae International"), Axum, Concept Gifts, Concept Gifts (M) Sdn Bhd, Edge Point (M) Sdn Bhd and Edge Point (S) Pte Ltd;

(f) The first and second defendants conspired with the third defendant to make to the third defendant the fraudulent payments described in paras (b) and (c) above.

5 Against the third defendant, the plaintiff's allegations may be summed up as follows:

(a) He conspired with, aided and abetted the first and second defendants in the dissipation of the assets of the Company, in particular by his receiving moneys as purported salaries, bonuses and loans;

(b) He conspired with, aided and abetted the first and second defendants, and was knowingly a party to the fraudulent conduct of the business of the Company to defraud the plaintiff, in particular:

(i) by the setting up of Amrae Sdn Bhd, Amrae International and Axum and transferring to them goods bought by the Company from the plaintiff without the Company or the plaintiff being paid for the same;

(ii) by the transferring of goods (bought by the Company from the plaintiff) to Concept Gifts (of which the third defendant was sole proprietor but which was later converted into a private limited company owned by the three defendants) without the Company or the plaintiff being paid for the goods.

6 The defendants were able to show that some of the allegations arose out of the plaintiff's misinterpretation of accounting entries. For example,

(a) the loans which the first and second defendants were alleged to have caused the Company to grant to themselves and to the third defendant were in fact payments of outstandings owed by the Company to the defendants in respect of accrued directors' fees and/or loans made by the defendants to the Company; and

(b) the $283,769.31 (allegedly spent on advertising and promotion in 2002 when the Company was insolvent) was shown to have been incurred previously, accounting adjustments having been made belatedly in 2002.

Others were explained away with apparent certitude by the defendants. The plaintiff was unable to adduce any evidence to controvert such explanations even if they were not accepted.

7 The payments of salaries, travelling expenses and bonuses were not denied. However, it was shown that the salaries and travelling expenses were substantially the same as for the years since the Company started business. The plaintiff's witness had said that if it were less, he would not have objected. When pressed, he did not suggest what the lower figure might be. Mr Suppiah intervened to say that it was a point for submission but this was not pursued in closing submissions. Indeed, in closing, Mr Suppiah said:

> There are many facts in this case which are not materially relevant and they have been set out in paras 9, 10, 11, 12 and 13(1), (3) and (4) of the Re-Amended Statement of Claim.

When I sought clarification on this, he said that the plaintiff would only be "targeting" the sale of $1,268,983 worth of goods by the Company to Axum. That is set out in para 13(3) of the Re-Amended Statement of Claim in the following terms:

> The 1st and 2nd Defendants together with the 3rd Defendant, incorporated on or about 4.6.2001 a company called Axum Marketing Pte Ltd (Axum) and caused the subject Company to transfer goods bought from the Plaintiff to the said Axum for the purported value of $1,268,983.02. No payments have been made by this Company to the said subject Company.

8 From the evidence, it is clear that the Company had a long course of dealings with David Chan Chon Tuck ("Chan") and (from October 1994) Niklex, which was at all times represented by Chan. It is common ground that:

(a) "There was a great deal of trust" between the first and second defendants and Chan;

(b) During this period of ten years, the Company made regular periodic payments on a running account although invoices were given between three and 24 months after deliveries;

(d) In all, the Company paid the plaintiff more than $5.2m during this ten-year period;

(d) Chan/Niklex gave the Company generous credit terms. (Although Chan initially denied this, he did concede that the Company was given credit of $0.5m);

(e) From 1994, Chan had access to the Company's profit and loss account and balance sheet to determine his share of profits as a *de facto* shareholder as to 50% of the Company's shares. (However, he said vouchers, invoices and bank statements for the period 1992 to 1998

had not been given to him.)

9 The first defendant's affidavit of evidence-in-chief gave a fairly detailed account of the deterioration in the relationship between Chan and the first and second defendants from 1998 onwards. In brief:

(a) Chan demanded an increase of his share in the Company to 60% to which the first and second defendants reluctantly agreed;

(b) Chan regularly inspected the accounts books in the company's office and took the Company's payment vouchers and GST quarterly submissions for review;

(c) He queried the Company's expenses, what the Company purchased and the sources of supply;

(d) The first and second defendants complained of uncompetitive prices and unreliable delivery of goods;

(e) Chan, by deception, caused the Company to give up, in favour of the plaintiff, the distribution of Preciosa Crystal figurines to certain department stores;

(f) The first and second defendants feared that Chan's agenda was ultimately to take away their business by supplying directly to the department stores, the Preciosa Crystal incident being merely a precursor;

(g) The first and second defendants realised that if they continued to buy from Chan they would not be able to compete in the market. (Since 1997, with major political changes in Czechoslovakia and the privatisation of the Czech factories, any large buyer could buy Bohemia crystalware from factories in the Czech and Slovak Republics at better prices than before. Bohemia crystalware prices fell steadily until 2002 at the earliest);

(h) Chan insisted nevertheless that they should continue to buy from the plaintiff and that they could gradually pay him for the goods supplied earlier;

(i) In 1999, when the Company owed the plaintiff about $1.5m, Chan demanded an increase of his stake in the Company to 70% and also asked for a salary. After much negotiation, the parties agreed to the increase to 70% but without a salary for Chan.

10 Then followed the meeting(s) around February 2000 between Chan and the first and second defendants. Chan recalled two meetings (one at McDonald's at Kallang Place and the other at Cuppage Centre) whereas the first and second defendants recalled only the meeting at Cuppage Centre. Their recollection of what transpired at the meeting(s) also differed in one particular, *viz*, how the outstandings owed to the plaintiff were to be repaid. Whereas the first and second defendants asserted that it was agreed with Chan that the Company would repay by instalments spread over three years, Chan insisted that he had not agreed. (In his letters of 31 January 2001 and 31 March 2001 to the Company, apart from denying that he had agreed to accept instalment payments, he called upon the Company to make payment of the amounts outstanding.) What is clear though is that the Company made 14 instalment payments aggregating $720,000 from April 2000 to July 2001. According to the first and second defendants, they stopped paying thereafter because (a) there was a dispute as to the amount outstanding; and (b) Chan insisted that he had not agreed to payment by instalments.

11 It is also not in dispute that:

(a) During the discussion at Cuppage Centre, the first and second defendants proposed to Chan that they be allowed to cancel the December 1999 order and also to return all unsold stock previously bought from the plaintiff if the plaintiff wanted the Company to run down the outstanding debts; and

(b) This was rejected by Chan.

This December 1999 order turned out to be the last purchase order that the Company made and the goods ordered were delivered sometime in February or March 2000 (or, as the second defendant recalled in his evidence, in March and April 2000).

Fraudulent trading

12 Section 340(1) of the Act provides as follows:

> If, in the course of the winding up of a company or in any proceedings against a company, it appears that any business of the company has been carried on with intent to defraud creditors of the company or creditors of any other person or for any fraudulent purpose, the Court, on the application of the liquidator or any creditor or contributory of the company, may, if it thinks proper to do so, declare that any person who was knowingly a party to the carrying on of the business in that manner shall be personally responsible, without any limitation of liability, for all or any of the debts or other liabilities of the company as the Court directs.

In order to succeed under this section, the plaintiff will need to prove two elements, *viz*:

(a) that the business of the Company has been carried on with intent to defraud the creditors of the Company or of any other person or for any fraudulent purpose; and

(b) that the defendants were knowingly parties to the carrying on of the business in that manner.

"Defraud" and "fraudulent purpose" connote "actual dishonesty involving, according to current notions of fair trading among commercial men, real moral blame": see *In re Patrick and Lyon, Limited* [1933] Ch 786 at 790.

13 In *Welham v Director of Public Prosecutions* ("*Welham*'s case") [1961] AC 103 at 123, Lord Radcliffe said:

> Now, I think that there are one or two things that can be said with confidence about the meaning of this word "defraud". It requires a person as its object: that is, defrauding involves doing something to someone. Although in the nature of things it is almost invariably associated with the obtaining of an advantage for the person who commits the fraud, it is the effect upon the person who is the object of the fraud that ultimately determines its meaning.

Elaborating on this, he approved that part of Buckley J's *dicta* in *In re London and Globe Finance Corporation, Limited* [1903] 1 Ch 728 at 733 where the learned judge said "to deceive is by falsehood to induce a state of mind; to defraud is by deceit to induce a course of action". In the same vein, Lord Denning in *Welham*'s case at 133 said:

> "To deceive" here conveys the element of deceit, which induces a state of mind, without the element of fraud, which induces a course of action or inaction.

Thus, in *R v Grantham* [1984] QB 675 at 683, Lord Lane CJ, in upholding a conviction for fraudulent trading, had this to say:

> In the present case it was open to the jury to find, if not inevitable that they would find, that whoever was running this business was intending to deceive or was actually deceiving [the supplier] into believing that he would be paid in 28 days or shortly thereafter, when they knew perfectly well that there was no hope of that coming about. *He was plainly induced thereby to deliver further potatoes on credit*. The potential or inevitable detriment to him is obvious. [emphasis added]

14 The mere preference of one creditor over another will not suffice. Thus in *In re Sarflax Ltd* [1979] Ch 592, the directors of a company who knew or had reason to suspect that the company would not be able to pay all creditors in full, did not have an "intention to defraud" merely by their preference of one creditor over another. The facts of the case are of some interest and I take the liberty of adopting the summary thereof in the headnotes:

> In 1966 the company entered into a contract governed by the law of Italy, to supply to an Italian company, SAFE, a particular type of press. When delivered the press did not work satisfactorily, and a dispute arose between the parties. In October 1970 SAFE started proceedings in the Queen's Bench Division claiming some £80,000 damages, but these proceedings were allowed to lapse after the company had entered an appearance under protest and the question of jurisdiction was not determined. In October 1971 SAFE commenced proceedings for damages in the Italian courts at Turin. The company took no part in these proceedings and judgment was entered against it in November 1973 in the sum of 120,465,690 lire, ie, about £86,000. In the meantime, the company, pursuant to a resolution passed in January 1971, had ceased to trade as from the close of business on April 30, 1971. The company was a wholly owned subsidiary of F Ltd to which it had become substantially indebted. When the company ceased trading its fixed assets, stock-in-trade and work in progress were sold to F Ltd at book value, the price paid by F Ltd being set off against the company's indebtedness to F Ltd. There was no suggestion that the price paid was other than a proper one or that the company's indebtedness to the parent company was otherwise than bona fide incurred in the course of trade. Over the next two years the remaining assets of the company were got in and applied in discharging the company's established debts, but without taking account of the pending claim by SAFE. On September 23, 1973, a resolution was passed for a voluntary winding up and the applicant was appointed liquidator. After receipt of the judgment of the Italian court, the liquidator admitted SAFE's proof of debt in the liquidation.
>
> By a summons, dated November 12, 1975, under section 332(1) of the Companies Act 1948 the liquidator sought a declaration that from January 13, 1971, to September 7, 1973, business had been carried on with intent to defraud creditors and in particular SAFE in that F Ltd, well knowing that the company was unable to pay its debts in full caused the assets of the company to be distributed amongst creditors other than SAFE to the intent that such creditors should be preferred to SAFE. Two persons who were formerly directors and principal shareholders both of the company and of F Ltd were made respondents to the summons.

It was held, *inter alia*, that when the only allegation was the bare fact of preferring one creditor over another, it was impossible to hold that such preference *per se* constituted fraud within the meaning of s 332 of the UK Companies Act 1948 (c 38) (the progenitor of s 340(1) of our Companies Act).

Counsel for the liquidator had argued that whatever might be the position regarding other creditors, the preference of the debt due to the parent was on a different footing. Oliver J, however, held that the preference of the parent was no different from the preference which occurred in *In re Lloyd's Furniture Palace, Limited* [1925] Ch 853 where the preferred creditor was himself a director and shareholder and indeed the promoter of the company. (Nevertheless, Oliver J did leave open the question whether there might be circumstances of a very peculiar nature involving preferential payments from which the intention required by s 332 could be inferred.)

15 Coming now to the present case, what are the facts which could point to an intention to defraud? Over the years the Company had purchased goods from the plaintiff on a running account under which credit was given to the Company. The last purchase order was in December 1999. The first and second defendants had tried to cancel the purchase order but Chan had refused to allow it. Neither did he accept their offer to return goods so as to reduce the outstanding amount owed to the plaintiff. Up to the time of delivery of the goods purchased under the last purchase order, the Company had remained solvent if only because the plaintiff allowed the running account to continue.

16 Although Chan had alleged in his affidavit of evidence-in-chief that the Company had been insolvent since 1999, he conceded under cross-examination that the Company was not insolvent for the financial years ending 31 March 1998, 1999 and 2000 as there was an excess of assets over liabilities in respect of each of the years. He further agreed that Niklex was practically the sole creditor and that, if at anytime during the three years Niklex had demanded payment in full, the Company would not have been able to pay promptly. Nevertheless, until such time that the plaintiff made a demand for the moneys owing and the Company failed to pay, it could not be said that the Company was insolvent: *Re Great Eastern Hotel (Pte) Ltd* [1988] SLR 841.

17 There is no evidence to suggest that at the time they obtained goods from the plaintiff, the first and second defendants had any intention that the plaintiff should not be paid or that they had no reasonable expectation of eventually being able to pay for the goods. Any suggestion of dishonesty is immediately and effectively met with the riposte that the first and second defendants had offered to cancel their last purchase order and to return to the plaintiff goods as yet unsold which they had previously bought from the plaintiff. Besides, over the years, they had paid the plaintiff more than $5.2m for the goods they had purchased. Even after the parting of ways following the Cuppage Centre meeting in February 2000, they had paid $720,000 to the plaintiff by instalments stretching from April 2000 to July 2001. It also emerged that some of the money with which the Company paid the instalments came from loans made to the Company by the defendants. Whether or not one believes their reasons for discontinuing payment thereafter (and I should add that I did not find the reasons convincing), the fact remains that there is no evidence to justify a finding of intent to defraud when the Company obtained goods from the plaintiff.

18 I move on to events after the parting of ways following the Cuppage Centre meeting. The plaintiff alleged, though not in so many words, that:

(a) with intent to defraud the plaintiff, the first and second defendants wrongfully transferred to Axum the Company's assets in order to put them out of reach of the plaintiff; and

(b) the third defendant conspired with and aided and abetted the first and second defendants in the wrongdoing.

19 Axum was bought as a shelf company by the defendants in June 2001 and started trading in July 2001. The first and second defendants explained that the setting up of Amrae International and Axum was a way of resolving differences that had arisen between the first and second defendants as

to the running of the Company. The solution found was that although they (together with the third defendant) would be shareholders and directors in the two companies, the first defendant would be responsible for the running of Amrae International (which would concentrate on the export market) while the second defendant would run Axum (which would concentrate on the domestic market). Under cross-examination, the first defendant also offered this explanation when he was asked why it was necessary to form Axum:

> We had a sort of "partnership" with David Chan and Niklex had asked for full payment from Amrae. So we felt that he would wind up Amrae. In order to survive and also to meet all our obligations, we would have to have another vehicle to trade.

20 Although the second defendant did not agree with the first defendant that they were afraid the plaintiff would wind up the Company, he confirmed that a new vehicle was needed to obtain goods from new suppliers at cheaper prices and thereby earn better profits from which they would be able to pay off all debts eventually.

21 Between July 2001 and June 2002, the Company sold Axum goods worth $1,268,983.02 on credit under a running account. Both the first and second defendants denied that the goods of the Company were moved out to Axum in order to defeat the plaintiff's claims and insisted that Axum bought the goods at arm's length prices. In para 20 of his affidavit of evidence-in-chief, the second defendant stated that 99% of the goods that Axum bought from the Company were at prices at least 10% higher than what the Company paid for them. This was not challenged by the plaintiff. The Company gave Axum credit notes in the amount of $114,246.73 for goods returned to the Company. Axum paid a total of $713,831.38 to the Company.

22 Therefore the plaintiff's allegation that the goods were sold by the Company to Axum for no payment was untrue. It is true though that none of the $712,831.38 received by the Company was paid over to the plaintiff. This, despite the second defendant's evidence that in setting up Axum, the first and second defendants were intending to pay off the outstandings owed to the plaintiff. What happened to the money then? In answer to this question by Mr Suppiah, the first defendant answered:

> There were a lot of moneys loaned to Amrae by Concept Gifts, second defendant, third defendant and myself. We took money out from Amrae to invest in Axum (actually loaned to Axum) so that we could trade profitably and thereby repay plaintiff.

23 The Company could have used the money to keep up instalment payments to the plaintiff but did not. I am not persuaded by the first and second defendants' reasons for stopping the instalment payments. In my view, at the time these repayments of loans were made, the Company was already insolvent, the plaintiff's demand of 31 January 2001 not having been met. A case could well be made out for saying that in making these and other payments (such as the payment of directors' fees accrued from previous years) the company was unfairly preferring the defendants over the plaintiff. In many instances, as shown in the defendants' document marked "DD-3", moneys paid by the Company to the defendants were channelled (by way of loan or otherwise) into Axum which then paid the moneys the same day, or shortly thereafter, over to the Company to run down the outstandings owed by Axum to the Company. The moneys simply went one full circle. However strongly suggestive of unfair preference they may be, the facts are insufficient, in my view, to warrant a finding that the defendants are liable for fraudulent trading under s 340(1). Harking back to the judicial pronouncements in *Welham's* case ([13] *supra*) as to the meaning of "defraud", it is difficult to see what course of action or inaction on the plaintiff's part such preference was intended to induce.

24 There was nothing in the evidence to bring this case within the penumbral region alluded to by Oliver J in *In re Sarflax Ltd* ([14] *supra*), where preference in very peculiar circumstances might permit an inference of an intention to defraud.

25 Similarly, Chan's allegation that the first and second defendants conspired with the third defendant was not made out. No evidence of any conspiratorial agreement or arrangement was adduced. It was held in *Seagate Technology Pte Ltd v Goh Han Kim* [1995] 1 SLR 17 that the essence of a conspiracy is an agreement and that there has to be proof of the existence of an agreement or, at least, an arrangement between the alleged conspirators to defraud. It was further held that a high degree of proof is required. In the present case, there was nothing more than a bare allegation. This will not suffice.

26 At this juncture I should add a few remarks regarding the expert evidence of Lau Kau Chin. I regret to say that I found his evidence to be of no assistance to the court. His affidavit of evidence-in-chief of 17 May 2004 and supplementary affidavit of evidence-in-chief of 29 August 2004 did not comply with O 40A r 3 of the Rules of Court (Cap 322, R 5, 2004 Rev Ed). No written report was furnished and, accordingly, there was no statement that he understood that in giving his report, his duty was to the court and that he complied with that duty. Indeed, it seemed clear to me that his affidavit of evidence-in-chief of 17 May 2004 was little more than a regurgitation of the plaintiff's case. Paragraph after paragraph of the expert's affidavit of evidence-in-chief merely repeated the averments of the plaintiff in the statement of claim. Although a "corrective affidavit" was later sworn on 30 August 2003 seeking to remedy the omission of the said statement prescribed by O 40A r 3(2)(h), this did nothing to allay the court's fears. His evidence being so obviously partisan, no later affidavit could cure the defect.

27 Accordingly, *albeit* with some regret, I dismiss the plaintiff's claim. It is still open to the plaintiff to request the Official Receiver (or any other liquidator appointed in his stead) to consider instituting proceedings against any creditors who may have been unfairly preferred for the recovery of moneys paid by the Company. I am unable to say more as the question whether or not there had been unfair preference was not before me.

28 I will hear the parties on costs.