Chaly Chee Kheong Mah, Po'ad bin Shaik Abu Bakar Mattar & 34 others practising in the name and style of Deloitte & Touche v The Liquidators of Baring Futures (Singapore) Pte Ltd [2002] SGHC 273

Case Number	: CWU 246/1995 (No 2), M Nos 600141 & 600142 of 2001
Decision Date	: 19 November 2002
Tribunal/Court	: High Court
Coram	: Lai Kew Chai J
Counsel Name(s)	: Haridass Ajaib/Randhir Chandra [Haridass Ho & Partners] for the applicant; V K Rajah, SC/Chong Yee Leong/Deanna Seow [Rajah & Tann] for the respondent
Parties	: Chaly Chee Kheong Mah, Po'ad bin Shaik Abu Bakar Mattar & 34 others practising in the name and style of Deloitte & Touche — The Liquidators of Baring Futures (Singapore) Pte Ltd

Court in England, in which judgment was given in its favour; (b) the legal costs incurred by it in defending proceedings brought against one of its partners before the Singapore Public Accountancy Board, in which judgment was given in its favour; and (c) the legal costs incurred by it in defending proceedings brought against it by BFS in the High Court in England, in the event that judgment was given in its favour. D&T Singapore also contended that all sums payable to it in respect of the indemnity referred to in (c) are payable out of the assets of BFS in priority to all other claims or, as an expense of the liquidation in priority to the claims of all creditors entitled to prove in the liquidation.

Article 110 provided that every director or other officer of the Company shall be entitled to be indemnified out of the assets of the Company against all losses or liabilities, which he may sustain or incur in or about the execution of the duties of his office or otherwise in relation thereto.

Three issues arose in this application: Firstly, whether Article 110 was incorporated into the contract between BFS and D&T Singapore; secondly, whether or not Article 110 covered the costs of successfully defending legal proceedings; and thirdly, whether the indemnity element in respect of D&T Singapore's costs for the BFS action should be treated as an Expense claim and accorded priority.

Held, dismissing the motions:

BFS's Articles of Association were not part of the contract between BFS and D&T Singapore. The established position at law is that the Memorandum and Articles of Association bind only the company and its members inter se and not third parties including auditors. Though generally the articles may be a source of the terms of engagement, it was not right to assume that they are incorporated into the engagement of every auditor (See [24] and [26]).

In this case, it cannot be reasonably concluded from the two letters of 6 and 15 October 1986 that Article 110 was incorporated into the contract of engagement. Firstly, the letter of 6 October was a formal request to seek D&T Singapore's consent to be appointed as auditors. Although BFS enclosed its Memorandum and Articles of Association under the cover of the 6 October letter, it had to be noted that the Articles were sent 'for the information' of D&T Singapore. The more important letter was that of 15 October, in which there was no reference to the earlier letter of 6 October, let alone the Memorandum and Articles of Association. (See [22] and [25]).

Article 110 was not intended to cover the expenses incurred by D&T Singapore in defending proceedings against it. This was because Article 110 was amended from its equivalent, which was Article 113 in Table A of the Fourth Schedule to the Companies Act, to remove the original wording in Article 113 that expressly

provided for indemnification of the costs for successfully defending proceedings. As a result of the amendment, Article 110 was couched in general language which cannot cover indemnification of expenses incurred in defending legal proceedings. Costs incurred by D&T Singapore in defending legal proceedings brought against it for acts which would be against its duty to do, were not losses or liabilities sustained by it in or about the execution of its duties to BFS or otherwise in relation thereto (See [30] – [37]).

For a debt accruing post-liquidation but under a pre-liquidation contract to be elevated in priority based on the "liquidation expenses" principle, it had to be shown that the debt was incurred for the benefit of the estate. The costs incurred by D&T Singapore in defending the proceedings and BFS's liability for the same (if any) under a pre-liquidation contractual obligation could not be described as expenses incurred by BFS for the benefit of the estate. It was undeniable that the potential liability to D&T Singapore's costs under Article 110 was a risk which had been imposed on the BFS liquidations by the pre-liquidation contract and was certainly not incurred for the benefit of the estate (See [43]).

D&T Singapore should not be awarded indemnity costs by the English court in the BFS action to reflect the Article 110 contractual entitlement, as that would upset the priorities in the liquidation of BFS which was under the supervision of the Singapore courts. D&T Singapore would not be entitled to "super-priority" in respect of the indemnity element of any costs awarded on an indemnity basis solely to reflect D&T's contractual entitlement under Article 110. The indemnity element of costs under Article 110 should accordingly not be treated as an Expense claim (See [44]).

Case referred to

John v Price Waterhouse and another

[2001] All ER (D) 125 (Jul) (refd)

Kahn & Anor v Commissioners of Inland Revenue

[2002] UKHL 6 (refd)

Re Atlantic Computer Systems PLC

[1992] Ch 505 (refd)

Re City Equitable Fire Insurance Company

[1925] Ch 407 (refd)

Re Famatina

[1914] 2 Ch 271 (refd)

Rowland & Ors v Gulfpac Limited

[1999] Lloyd's Rep Bank 86 (refd)

Tomlinson v Adamson

(1935) SC 1 (refd)

Legislation referred to

Companies Act (Cap 50), s 172

Judgment

Cur Adv Vult

GROUNDS OF DECISION

Introduction

1 Massive losses were incurred as a result of the criminal and fraudulent activities of a rogue trader in Baring Futures (Singapore) Pte Ltd ("BSF"). The funds were provided by its parent, Barings PLC ("PLC") of London, and the losses brought about the collapse of the Barings group. PLC, BSF and their related company Bishopscourt (BS) Limited, formerly known as Barings Securities Limited ("BSL"), acting by their respective liquidators, instituted or continued with legal proceedings to recover damages from Deloitte & Touche, Singapore ("D&T Singapore") and Coopers & Lybrand, Singapore ("C&L Singapore") and Cooper & Lybrand, London ("C&L London"). D&T Singapore and C&L Singapore were successively auditors of BFS. The claims against D&T Singapore and C&L Singapore are essentially for negligence in the audit of the accounts of BSF and also in the audit of BFS's consolidation schedules under the United Kingdom auditing standards for group accounts. The proceedings in the High Court in London against D&T Singapore have proceeded to an advanced stage. But I was told that it was estimated to continue into the first half of 2003. The liquidators of BSF could continue with their litigation against D&T Singapore because of the escrow funds which were set aside out of the settlement sums paid by C&L Singapore and C&L London who settled with the Barings group. The settlement will be elaborated later in this judgment.

2 However, the amount of legal expenses which D&T Singapore had incurred is, according to them, in the order of some 30 million and, in the circumstances, both the liquidators of the three companies and D&T Singapore are very keen to have a determination from this court, notwithstanding what I had stated in my judgment which was reported in [2002] 1 SLR 370. Both parties agreed that I should make my determination and set out my views on the issues raised.

3 I have two motions before me. They are predicated on the assumption that D&T Singapore eventually succeeds before the courts in London in defending the claims for negligence. In these applications, D&T Singapore claim, in effect, that their legal costs calculated on an indemnity basis, and not merely on the standard basis, should as a matter of priority rank in the liquidation of all three companies as an expense, by reason of either or both of the estate costs rule and the liquidation expenses principle, whatever is the appropriate categorisation.

The background

4 D&T Singapore was appointed auditor of BSF on 15 October 1986 by a resolution of the directors of BSF. As usual in the appointments of auditors, the firm was re-appointed to the office of auditor for each successive year until 1994. In and from that year, C&L Singapore was appointed the auditor and was an officer of BSF from that date until about July 1994.

5 The precise circumstances and terms of the appointment of D&T Singapore as the auditor are relevant. By a letter of 6 October 1986 the solicitors of BFS wrote to D&T Singapore (then known as Deloitte Haskins+Sells). The letter was in these terms:-

> "6th October 1986
>
> M/s DELOITTE HASKINS & SELLS
>
> 6 Battery Road
>
> #27-01 Standard Chartered Bank Building
>
> Singapore 0104
>
> ATTN: MR OWEN Y. LEE
>
> Dear Sirs

BARING FUTURES (SINGAPORE) PTE LTD – "THE COMPANY"

The Company wishes to appoint your firm as its auditors and this is a formal request to seek your consent.

The Company was incorporated on 17th September 1986 with an authorised capital of ...(illegible in part)... shares of S$1/- each were issued and fully paid up.

We enclose a copy each of the following documents for your information:-

1. Certificate of Incorporation (FORM 9)

2. Memorandum and Articles of Association

3. FORM 49 showing the particulars of the directors

We look forward to your early reply.

Yours faithfully

(Sgd) "

6 By a directors' resolution passed on 15 October, 1986 it was resolved that subject to its written consent to act as auditor, D&T Singapore be appointed auditor of the company and to act as such until the first Annual General Meeting of the company at a remuneration to be thereafter determined.

7 On 15 October 1986, D&T Singapore wrote to the Board of Directors of BFS confirming its consent to act as auditor for the company. The letter stated:-

"The Board of Directors October 15, 1986

Baring Futures (Singapore) Pte Ltd

24 Raffles Place, $24-01/04 Ref: PM/sl

Clifford Centre

Singapore 0104

Dear Sirs,

APPOINTMENT OF AUDITORS

We are pleased to confirm our consent to act as auditors for your company pursuant to Section 10 sub-section 7 of the Companies Act, Cap. 185.

Until advised to the contrary, please accept this letter as our consent to act in future years.

Sgd

PO'AD MATTER

PARTNER "

8 I was also shown another letter written by D&T Singapore and also dated 15 October 1986. It was post-contractual. It is best that I set the terms of the letter in full, which are as follows:

"The Board of Directors October 15, 1986

Baring Futures (Singapore) Pte Ltd

24 Raffles Place, $24-01/04 Ref: PM/sl

Clifford Centre

Singapore 0104

Gentlemen,

Following our appointment as auditors of the company we are writing to confirm our responsibilities as auditors, and also our understanding of the other services that we should perform.

1. AUDIT

We will act as auditors in examining and reporting on the company's annual accounts in compliance with the Companies Act, Cap. 185.

The directors are responsible for preparing financial statements that give a true and fair view, and for maintaining proper accounting records and an appropriate system of internal control.

Our function as auditors under the Companies Act, Cap. 185 is to examine the statutory accounts prepared by the directors as well as the related accounting records and ...(illegible in part)... as required by the Act. Our examination will be made in accordance with auditing standards generally accepted in Singapore.

To enable us to express our opinion, we shall make such tests and enquiries as we consider necessary. The nature and extent of our tests will vary according to our assessment of the company's systems of internal accounting control. We shall report to the directors or to the appropriate level of management any material weaknesses in the company's systems of internal accounting control which come to our notice and which we believe should be brought to their attention.

Our audit is designed, in accordance with normal practice, to enable us to express an opinion on the accounts. It should not be relied upon to disclose defalcations or other irregularities, although their disclosures, if they exist, may well result from the audit tests we undertake.

The foregoing does not cover maintaining the accounting records and the preparation of accounts, these being the responsibility of the company's directors.

2. ACCOUNTING AND OTHER SERVICES

It was agreed that we should carry out certain accounting services, namely:-

a. To prepare final accounts under your direction and responsibility from draft accounts prepared by the company's staff for approval by the Board of Directors.

b. To type and print the financial statements and the directors' report.

It was agreed that we will act as financial advisers any matters which you refer to us.

3. TAXATION SERVICES

We will also assist you with the following taxation services as your tax agents.

- To review the company's computation of the provision for taxation for inclusion in the ...(illegible in part).
- To prepare the company's income tax returns and to submit them to and agree them with the Comptroller of Income Tax, subject to prior reference to you for your approval.
- To act as your taxation advisors on all matters which you refer to us.

In this regard, we attach a specimen appointment letter addressed to The Comptroller of Income Taxes and would be grateful if you would complete such a letter on the company's letterhead and send the completed letter together with two copies for us to process and onwards transmit to the Comptroller.

4. FEES

Our fees are computed on the basis of the time necessarily occupied on your affairs by partners and staff of different seniority depending on the degree of responsibility, scope and skill involved.

Our fees and the related out-of-pocket expenses will be charged separately for each of the main classes of work mentioned above. We shall bill our fees and out-of-pocket expenses on a periodic basis during the engagement and we shall agree the frequency and amount of such billing with you and you agree to observe our payment terms.

We shall be grateful if you will kindly sign and return to us the duplicate of this letter as acknowledgement of your understanding of the terms of our engagement which will continue to apply until varied by a subsequent letter. However, if there are any aspects of our letter which are not in accordance with your requirements, we shall be pleased to discuss them with you.

We, at Deloitte Haskins & Sells look forward to serving you.

Yours truly,

DELOITTE HASKINS & SELLS

(Sgd)

PO'AD MATTAR

PARTNER "

9 The various actions against C&L Singapore and C&L London (collectively referred to as "C&L") were settled in October 2001. C&L paid 65 million in settlement of the claims brought against it by BSF, PLC and BSL. BSF's share was 28 million. After that settlement BSF had 38.2 million, out of which it contributed 35.75 million towards the settlement of the creditors' claims against the Barings group. BFS retained the balance to fund liquidation costs.

10 Under an Escrow Agreement reached, the sum of 32.5 million was set aside to fund the continuation of the actions against D&T Singapore. Of this amount, the sum of 24 million constituted the "Costs Escrow Account", intended to meet any costs in favour of D&T Singapore and the sum of 8.5 million funded the "Litigation Escrow Account" which was intended to meet the costs of the BFS, PLC and BSL liquidators as to 6 million for BFS and as to 2.5 million for PLC and BSL combined. The Litigation Escrow Account is to be used for specified purposes which included the BFS, PLC and BSL liquidators' costs of continuing the action against D&T Singapore in London. The Costs Escrow Account was put in place because BFS accepts that, as a matter of general principle, any adverse cost orders made against BFS would be a liquidation expense ranking above all other liquidation expenses save for those incurred in getting in, maintaining and realising the assets of the company.

11 The action against D&T Singapore brought by PLC and BSL was struck out by order of Evans-Lombe J in December 2001. The appeal to the Court of Appeal is, I am told, stayed.

D&T Singapore two motions

12 By a Motion in this Winding-Up petition D&T Singapore asked that the decision of the liquidators of BFS made on 5 December 2001, in rejecting the Proof of Debt dated 22 November 2001 in the liquidation be reversed and that it be ordered that the Proof of Debt be admitted in full. The first Proof of Debt included (a) its indemnity costs of the PLC action amounting to 3,286,901.35, which was a contingent claim; (b) its indemnity costs of the PAB proceedings amounting to 850,000 which was an actual claim for costs already incurred; (c) BFS's contribution liability in the third party action brought by D&T Singapore against BFS in the PLC action said to amount to a maximum of approximately 1.77 billion**,** a contingent claim; and (d) its costs of the BFS action amounting to a maximum of approximately 25,935,733.06 which was in part actual but mostly contingent. With regard to claims (a) and (b) D&T Singapore have accepted that these would be 'proof' claims ranking together with all other unsecured creditors of BFS and in respect of which a dividend would be payable on a pari passu basis. As regards claim (c) it was rejected by the liquidators of BFS on the ground, amongst others, that it related to a tortious unliquidated claim which is not proveable in liquidation.

13 D&T Singapore also asked that another decision of the liquidators of BFS in rejecting the Proof of Debt dated 7 December 2001 be reversed and that the said Proof of Debt be ordered to be admitted in full. In support of its application, D&T Singapore referred to the fact that it had incurred liabilities in respect of legal costs in defending proceedings brought by PLC and BSL in the High Court of England, Chancery Division and by the Singapore Public Accountancy Board ("the PAB proceedings"), in which judgment had been given in favour of D&T Singapore in both sets of proceedings.

14 D&T Singapore further pointed out that it had incurred and continued to incur liabilities in respect of legal costs in defending proceedings brought by BFS in the High Court of England, Chancery Division.

15 D&T Singapore contended that as 'officer' of BFS it was entitled to be indemnified out of the assets of the company pursuant to Article 110 of BFS's Articles of Association ("Article 110") in respect of any losses or liabilities that D&T Singapore may sustain or incur in or about the execution of the duties of its office or otherwise in relation thereto. It was further contended that the indemnity provided by Article 110 extended to costs incurred by it in defending proceedings in which judgment is given in its favour arising out of the execution of its office as auditor.

16 The primary case of D&T Singapore is that it is entitled to an indemnity in respect of the costs incurred by it in the legal proceedings in London instituted by BFS and that such indemnity ranks for payment in full as an expense of the liquidation of BFS. In the alternative,

D&T Singapore's entitlement to an indemnity in respect of the costs of that action is a provable debt and that the liquidators of BFS were wrong to have rejected its Proof of Debt dated 7 December 2001.

17 By the other Motion filed at the same time, D&T Singapore asked for a declaration that it is entitled, pursuant to Article 110 to an indemnity out of the assets of BFS in respect of:

> (a) the legal and other costs incurred by it in defending proceedings brought against it by PLC and BSL in the High Court in England in which judgment was given in its favour on 23 November 2002;
>
> (b) the legal and other costs incurred by it in defending proceedings brought against one of its partners, Chaly Mah Chee Keong, before the Singapore Public Accountancy Board, in which judgment was given in its favour by letter dated 16 November 2001; and
>
> (c) the legal and other costs incurred by it in defending proceedings brought against it by BFS in the High Court in England, in the event that judgment is given in its favour.

18 Further, D&T Singapore also sought a ruling as to the priority of its claims to the indemnity in the liquidation. The same grounds were relied upon. It sought a declaration that all sums payable to it in respect of the indemnity referred to in paragraph 15(c) above are payable out of the assets of BFS in priority to all other claims, including that of the liquidator for his own legal costs and remuneration, alternatively as an expense of the liquidation in priority to the claims of all creditors entitled to prove in the liquidation: (a) in the event that costs are awarded against BFS by the trial judge in the High Court in London on the indemnity basis (whether in order to reflect D&T Singapore's contractual entitlement under Article 110 or otherwise); and/or (b) in the event that costs are awarded against BFS by the trial judge in that action on the standard basis, such that D&T Singapore's entitlement to an indemnity arises solely under Article 110.

19 Article 110 provides as follows:

> "Every Director or other officer of the Company shall be entitled to be indemnified out of the assets of the Company against all losses or liabilities (including any such liability as is mentioned in the Act), which he may sustain or incur in or about the execution of the duties of his office or otherwise in relation thereto, and no such Director or other officer shall be liable for any loss, damage or misfortune which may happen to be incurred by the Company in the execution of the duties of his office or in relation thereto. But this Article shall only have effect in so far as its provisions are not avoided by the Act."

Incorporation

20 The first issue is whether Article 110 was incorporated into the contract between BFS and D&T Singapore. The first point to note is that on the terms of their letter of engagement dated 15 October 1986, as quoted above, the letter set out "the terms of our engagement which will continue to apply until varied by a subsequent letter". In *Re City Equitable Fire Insurance Company* [1925] Ch 407, there were no written terms of engagement between the auditors and the company but the auditors were found to have contracted on the footing of the articles. It was there recognised, and it is common ground in this case, that the articles constitute a contract between the company and its members but not as between the company and its auditors.

21 D&T Singapore, however, made the following points in relation to the letter of 15 October 1986. First, it pointed out that the letter is a post-appointment document and is a confirmation of the terms of an appointment already accepted. Secondly, it was submitted on its behalf that the letter did not purport to be a comprehensive record of the terms of contract between BFS and D&T Singapore. As the range of services of an auditor was very wide, the fact that D&T Singapore specified its services is no reason to infer an intention to detract from

"terms otherwise incorporated generally into the contract". Lastly, D&T Singapore also pointed out that the letter was not a comprehensive record of the terms of contract between BFS and D&T Singapore, given in particular the absence of any reference to regulatory audit functions required of D&T Singapore. In response, BFS submitted that the first point raised irrelevant matters which did not disprove the fact that the accepted terms of the contract of appointment as expressly confirmed did not incorporate the Articles of BFS. The second point was, according to BFS, based on a flawed premise that there are other terms (namely, the Articles) generally incorporated into the contract. In relation to the last point, BFS contended that the absence of any reference to the regulatory audit functions of D&T Singapore was a neutral matter and did not advance the contentions of D&T Singapore in any way. Those functions, as a matter of contract, would be implied on the basis of necessity and making the contract of engagement work. That implication of the term as to audit functions is quite different from implying the contract under which BFS would indemnify D&T Singapore.

22 D&T Singapore further stressed the fact that BFS enclosed its Memorandum & Articles of Association under cover of their letter of 6 October 1986. On that fact, it submitted that the Articles were incorporated into the contract of appointment and relied on the case of *John v Price Waterhouse* [2001] All ER (D) 145 (Jul) where at paragraph 26 of the judgment Ferries J considered that "comparatively little will be required to satisfy the court that in particular cases, the indemnity provided for by regulations 136 and 118 is incorporated in the contract which is made when the company appoints a director or an auditor." In the context of this case, it has to be noted that the Memorandum and Articles of Association were sent ***'for the information'*** of D&T Singapore. The short letter stated the wish of BFS to appoint it as its auditors and the letter was a formal request to seek its consent. The letter went on to "enclose each of the following documents ***for your information***:- 1. Certificate of Incorporation (Form 9); 2. Memorandum and Articles of Association; 3. Form 49 showing the particulars of the directors" (emphasis added).

23 D&T Singapore further called in aid of their submission that Article 110 was incorporated into the contract by pointing out that the appointment to of a person to the office of auditor is an appointment to an office 'the attributes of which are (without more) defined in and subject to the applicable companies legislation and any applicable terms of the Memorandum and Articles of Association of the company'. It further noted that 'the appointment of an auditor necessarily carried with it certain attributes (including obligations and rights) that are to be found other than the specific terms of appointment.'

24 But must the attributes of the office be defined by and subject to the applicable terms of the Memorandum and Articles of Association? The general assertions of D&T Singapore as set out in the preceding paragraph may not be consistent with the established position at law that the Memorandum and Articles of Association bind only the company and its members inter se and ***not*** third parties including auditors. Admittedly, it is possible that a director or auditor may be employed by a company on the terms of its articles. In that case the articles will form part of the contract between the director or auditor and the company. This was the position in *Re City Equitable Fire Insurance Company* [1925] Ch 407, where there was no written terms of engagement between the auditors and the company but the auditors were found to have contracted ***on the footing*** of the articles. Warrington LJ at p527 pointed out that where "auditors are engaged without any special terms of engagement…then if the articles contain provisions relating to the performance by them of their duties and to the obligations imposed upon them by the acceptance of the office, I think it is quite plain that the articles must be taken to express the terms upon which the auditors accept their position. *Of course, if the terms of their employment are expressed in a separate document, then that document must be taken to define the conditions of their engagement, and it would not be proper to assume any implied terms either from the provisions of the articles or elsewhere."*

25 Both D&T Singapore and BFS agreed before me that all the evidence they had about the circumstances of the appointment of D&T Singapore are reflected in the two letters. On the basis of the two letters can one reasonably conclude that Article 110 was incorporated into the contract of engagement? In my view, the first letter was a 'formal' letter. The more important letter is the letter of 15 October 1986 quoted above. It should be noted that there is no reference to the earlier letter of 6th October, let alone the Memorandum & Articles of Association. Secondly, this letter was signed by Mr Po'ad Mattar who was the managing partner and not by Mr Owen Lee to whom the first formal letter was addressed by the solicitors of BFS.

26 I am persuaded by the submissions advanced on behalf of BFS and conclude that the articles were not part of the contract between it and D&T Singapore. The articles of a company constitute a contract between the members of the company inter se and between each of them and the company but, in the words of Ferries J in para 26 in the case of *John & Others v Price Waterhouse and another (supra)*, "do not, without more, constitute a contract between the company and its directors or auditors." Though generally the articles may be a source of the terms of engagement, it is not right to assume that they are incorporated into the engagement of every auditor. There was not, in this case,

sufficient material to conclude that BFS had agreed to confer on D&T Singapore the indemnity in terms of Article 110. The letter of 6 October 1986 signed by Mr Mattar was, in my view, not capable and did not incorporate the indemnity into the contract.

Scope of Article 110

27 I now turn to the second issue, namely whether Article 110 does not cover costs of successfully defending proceedings. BFS contended that D&T Singapore is not entitled to an indemnity in respect of its costs of the legal proceedings which its auditors had taken against it or the PAB proceedings. The reasons are these. First, and forcefully, BFS asserted that such costs are not losses or liabilities sustained or incurred by D&T Singapore in or about the execution of its duties to the company or otherwise in relation thereto. In addition or alternatively, it is argued on behalf of BFS that it was never intended by the parties that Article 110 would provide an indemnity for such costs. BFS expanded on these two cumulative or alternative bases in support of their proposition.

28 BFS relied on ***Rowland & Ors v Gulpac Limited*** [1999] Lloyd's Rep. Bank 86 (decided in 1995 but reported only in 1999). The Commercial Court in London considered, in the context of a Mareva injunction, an indemnity action brought by directors including Rowland against ***Gulfpac*** based on an article in ***Gulpac's*** articles in the following terms:

> "Subject to the provisions of the Act (viz the Companies Act 1985 of UK) ***every director, or other officer or auditor*** of the company, or person acting as an alternate director ***shall be entitled to be indemnified out of the assets of the Company against all*** costs, charges, expenses, ***losses or liabilities which he may sustain or incur in or about the execution of his duties to the Company or otherwise in relation thereto."*** (Emphasis added to show the similarity to BFS's Article 110).

29 Rix J (as he then was) considered that Rowland and the other directors could not establish a good arguable case for an indemnity from ***Gulfpac*** under Article 31 against any liability which they might incur as a result of proceedings being taken against them by ***Gulfpac's*** parent company, Gulf USA ("the Idaho proceedings") concerning (as the Judge found) "not…their role as directors of ***Gulfpac***, but only...their role as directors or offices of Gulf USA". He then addressed the question whether the directors were entitled to an indemnity as regards costs in the Idaho proceedings. After concluding that there was no indemnity for the liability complained of, he observed that it should follow that there would be no indemnity for costs, noting that the case of costs was "a fortiori". Rix J continued at p 93 lhc:

> "If the costs which are to be considered are costs ordered against the directors, then that might be viewed as a liability ancillary to the principal liability. In such a case costs and liability plainly go together. But ***costs incurred as an expense***, as occurs in the United States, where it is common there are no adversarial orders for costs, or in England as part of the directors' own English proceedings, ***are costs incurred in defending or prosecuting actions and are not,*** it seems to me, ***costs incurred or sustained in or about the execution of a director's duties*** to ***Gulfpac or otherwise in relation thereto.***" (emphasis added)

30 In paras 69 to 71 of its submissions D&T Singapore sought to distinguish the case by arguing that the above dicta was made by Rix J in the context of the actions against ***Gulfpac's*** directors being in connection with those directors' duties to ***Gulfpac's*** parent company and did not have anything to do with the execution of those directors' duties to ***Gulfpac*** itself. I agree with BFS that that was not a correct reading of the case. Clearly, Rix J was speaking in general of costs and held that costs incurred as an expense were costs incurred in defending or prosecuting actions and were not costs incurred or sustained in or about the execution of duties of the officer or otherwise in relation thereto.

31 Rix J stated that his view was fortified by two other considerations: see last paragraph on p 93 lhc and following. In referring to the first consideration, he said:

> "The first arises out of the terms of Section 310(3)(b) of the Companies Act 1985. Section 310(1) and (2) provides that any provision contained in a company's articles or in any contract with the company indemnifying an officer of the

company from any liability in respect of any negligence, default, breach of duty or breach of trust, is to be void. However, section 310(3) then provides as follows:

> 'This section does not prevent a company…
>
> (b) from indemnifying any such officer or auditor against any liability incurred by him,
>
> (i) in defending any proceedings, whether civil or criminal, in which judgment is given in his favour or he is acquitted…'

It seems to me that that ***subsection emphasises both by its function and by its language a liability for costs incurred in the successful defence of any proceedings is something different from a liability for costs sustained or incurred in the execution of the directors' duties to a company or, indeed, in relation thereto."*** (emphasis added).

32 It should be noted that the UK Section 310 referred to above is equivalent to Section 172 of the Singapore Companies Act which provides as follow:

> "172 (1) Any provision, whether in the articles or in any contract with a company or otherwise, for exempting any officer or auditor of the company from, or indemnifying him against, any liability which by law would otherwise attach to him in respect of any negligence, default, breach of duty or breach of trust of which he may be guilty in relation to the company, shall be void.
>
> (2) Notwithstanding anything in this section, a company may pursuant to its articles or otherwise indemnify any officer or auditor against any liability incurred by him in defending any proceedings, whether civil or criminal, in which judgment is given in his favour or in which he is acquitted or in connection with any application in relation thereto in which relief is under this Act granted to him by the Court."

33 To distinguish ***Gulfpac***, D&T Singapore submitted that it is not applicable because the wording of Article 110 is materially different from that in ***Gulfpac*** and that Rix J's comments were unnecessary for deciding the case before him where the facts were different. BFS, of course, asserted that ***Gulfpac*** is directly applicable to the present case and is very persuasive authority.

34 In relation to the second consideration, Rix J continued as follows:

> "The second matter which seems to me to fortify the conclusion to which I have arrived concerning "good arguable case" arises from the authority of ***Tomlinson v Adamson*** (1935) SC 1. That authority shows at least that the ***costs of successfully defending a prosecution for fraud does not easily come within a different version of an article 31 type indemnity.*** Whether or not the analysis in that authority is close, and granted that the wording of the provision there is probably narrower than article 31, the case does illustrate the ***difficulty of providing by general language for the indemnifying of a successful defendant.***" (emphasis added).

35 I agree with BFS that D&T Singapore faced the same difficulty. Article 110 was amended from its equivalent in Table A of the Companies Act, to ***remove*** the original wording in the article in Table A that ***expressly*** provided for indemnification of costs for successfully

defending proceedings. Article 113 in Table A in the Fourth Schedule of the Companies Act under the heading "Indemnity" reads as follows: Every Director...auditor…shall be indemnified out of the assets of the company ***against any liability incurred by him in defending any proceedings, whether civil or criminal, in which judgment is given in his favour or in which he is acquitted*** or in connection with any application under the Act in which relief is granted to him by the Court in respect of any negligence, default, breach of duty or breach of trust." (emphasis added). It should be noted that Table A was expressly excluded from BFS's Articles of Association. Further, the statutory words expressly providing for an indemnity against "liability incurred in defending any legal proceedings in which judgment is given in his favour or in which he is acquitted" were also excluded. There was accordingly no intention behind Article 110 to cover such expenses. At this stage, I should also note that Article 110 as a result of the amendments is couched in general language that cannot accommodate the meaning which D&T Singapore sought to ascribe to it.

36 In ***Tomlinson v Adamson*** (supra) the article in question was in the following terms:

> "Every Director…of the Company shall be indemnified by the Company against … all costs, losses, and expenses which any such Director … may incur or become liable to by reason of any contract entered into, or act or deed done by him as such Director…in any way, in the discharge of his duties, including travelling expenses."

37 In that case, the claimant director relied on the article and lodged with the liquidator a claim for his expenses in defending himself in criminal proceedings wherein he had been charged with issuing a fraudulent prospectus and fraudulently misapplying the company funds. He was acquitted of these charges. The liquidators rejected his claims. The director appealed to the court and maintained that he was entitled to be indemnified against the expenses (1) in virtue of the indemnity clause in the company articles, and (2) in any event at common law, as the expenses were incurred in consequence of acts done by him as agent of the company. The House of Lords, affirming the First Division, held that he was not entitled to his expenses. Lord Tomlin in the House of Lords stated in his judgment on p 6 as follows:

> "Here the allegation against the agent was that he had done something which he did not in fact do, and which would have been against his duty to do, are expenses incurred by him by reason of any act done by him as a director in the discharge of his duty. ***Upon the true construction of the article I am unable to see how that can possibly be maintained. In my view the expenses incurred by reason of the allegations made against (the director), being allegations of matters which would have been a breach of his duty and which were held to be disproved or non-proven, are not expenses incurred by him by reason of any act done by him as a director in the discharge of his duties.***
>
> If the cases does not fall, as I think it does not fall, within the language of article 160 of the articles of association, it is difficult to see upon what principle it can possibly be brought within the common law rule. My conclusion is that this appeal fails, and I recommend to your Lordships that it be dismissed with costs". (emphasis added)

38 D&T Singapore asserted in para 60 of its submissions that there is a direct causal link between the execution of its duties as auditor and the costs incurred by it in defending proceedings based on an alleged breach of those duties, so that such costs constitute a liability (if outstanding) or loss (if paid) incurred or sustained "in the execution" of D&T Singapore's dues as much as any expenses incurred by it in doing so. Even if this argument is wrong, D&T Singapore went on to say that such costs would have been undoubtedly incurred "otherwise in relation thereto" to the execution of its duties as auditor. D&T Singapore relied on the underlying proposition that if D&T Singapore was found to have breached its duties to BFS then there would be liability within the opening sentence of Article 110. In response, BFS pointed out with considerable force that it is quite clear from ***Tomlinson*** that any liability of D&T Singapore would ***not*** fall within the opening sentence of Article 110 because the relevant acts of D&T Singapore would not be within D&T Singapore's duty to do and therefore would not be acts done by D&T Singapore in discharge of its duty. Accordingly, any liability arising therefrom would not have been "incurred or sustained in the execution of D&T Singapore's duties or otherwise in relation thereto".

39 I now turn to D&T Singapore's reliance on the words in parentheses in Article 110 to distinguish the ***Gulfpac*** case. I am of the view that there is no difference in the distinction drawn. The words in parentheses are all qualified by the requirement that the liabilities of the officer be '***sustained or incurred in or about the execution of the duties of his office or otherwise in relation thereof.'***

40 Lastly, D&T Singapore sought to invoke the spirit of Article 110. It relies on ***Re Famatina*** [1914] 2 Ch 271 for the proposition that at common law there is no doubt that costs incurred by an agent in successfully resisting claims brought against it as a consequence of executing its duties are covered by the indemnity available to an agent under the general duty owed by a principal to its agent at law. D&T Singapore pointed out that the indemnity expressly permitted in Section 172(2) of the Companies Act is an aspect of this general duty. I do not think there is substance in this approach. It has been rightly pointed out that ***Re Famatina*** did not involve the agent having incurred the costs of successfully resisting proceedings brought by the principal itself. Secondly, House of Lords accepted the distinction between ***Re Famatina*** and ***Tomlinson*** on the facts and I also agree with BFS that the facts in ***Tomlinson*** are analogous to the present case to the extent that both cases involve the officer/agent having to defend proceedings brought against them for acts which would be against their duty to do. The director in ***Tomlinson*** had to defend himself against charges of fraud and D&T Singapore is defending against allegations of negligence.

Priority

41 Finally, I address the question whether the indemnity element in respect of D&T Singapore's costs for the BFS action should or should not be treated as an Expense claim and accorded priority. D&T Singapore pointed out that BFS's liability to D&T Singapore in respect of the costs of the BFS action will have been incurred by reason of the actions of the liquidators taken solely for the purpose of the winding up. It suggested that the simplest way to test this is to compare the situation at the commencement of the liquidation with the situation current in September this year. At the date of BFS's liquidation, whilst the indemnity provided by Article 110 existed, absolutely nothing was owing under it. As at September 2002, I was told, some 30 million is owned under it.

42 D&T Singapore argued that the indemnity under Article 110 survived the winding up of BFS on the basis of the estate costs rule or as the liquidation cost. There is, I am told, no Commonwealth authority where in an unsuccessful legal proceedings an order for indemnity costs were ordered against the liquidator. In my view I think that such an order would be wrong in principle; it would be an unwarranted departure from the pari passu rule.

43 If D&T Singapore were to succeed on this third and final issue, it would be on the basis of the estate costs rule or not at all. The liquidation expense rule, historically, was always meant to cover the usage of property by a liquidator. It has never been applied to costs. In this connection D&T Singapore relied ***re Atlantic Computer Systems PLC*** [1992] Ch. 505. BFS relies on ***Kahn & Anor v Commissioners of Inland Revenue*** [2002] UKHL 6, which disapproved of **Re Atlantic Computer Systems Inc.** It is clear from what was traversed in ***Kahn & Anor*** that for a debt accruing post-liquidation but under a pre-liquidation contract to be elevated in priority based on the "liquidation expenses" principle, it has to be shown that the debt was incurred for the benefit of the estate. Accordingly, costs payable to BFS's solicitors and experts incurred as a result of BFS choosing to bring proceedings against D&T Singapore could be said to have been incurred for the benefit of the estate of BFS. But the costs incurred by D&T Singapore in defending those proceedings is another matter altogether. I agree with BFS that it is not permissible to describe those costs of D&T Singapore, and BFS's liability for the same (if any) under a pre-liquidation contractual obligation, as expenses incurred by BFS for the benefit of the estate. It is undeniable that potential liability to D&T Singapore's costs under Article 110 should BFS lose its action against D&T Singapore is a risk which has been imposed on the BFS liquidators by the pre-liquidation contract and is certainly not incurred for the benefit of the estate.

44 I am persuaded to the view that D&T Singapore should not be awarded indemnity costs by the English Court in the BFS action to reflect the Article 110 contractual entitlement as that would upset the priorities in the liquidation of BFS which is under the supervision of the Singapore Courts. I have also concluded that D&T Singapore would not be entitled to "super-priority" in respect of the indemnity element of any costs awarded on an indemnity basis solely to reflect D&T's contractual entitlement under Article 110. I need hardly say that if the claims in the BFS action had been or would be misconducted (of which there is no evidence whatsoever) that would be entirely for the discretion of the trial Judge in London to consider awarding costs on an indemnity basis. But that is an entirely different matter, of which there is not a whiff of a suggestion that it would be in prospect. Accordingly, the indemnity element of costs under Article 110 should not be treated as an Expense claim.

45 In the premises, D&T Singapore's two applications are dismissed with costs.

Sgd:

Lai Kew Chai

Judge