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LEGAL INSIGHTS

A SKRINE NEWSLETTER

MESSAGE FROM THE EDITOR-IN-CHIEF

2012 is now upon us. There are many doomsday theories about 2012, including one which predicts that massive solar storms, earthquakes, super-volcanoes and other natural disasters will bring about the end of the world or human civilization. We will have no way of knowing whether these predictions will come true. Even if they do, we will not be around to know anyway. Hence, life must go on and in the 1st quarter of 2012, it has been good so far.

Readers will remember that our Malaysian Judiciary now has a new Chief Justice, Tan Sri Arifin Zakaria, who succeeded Tun Zaki bin Tun Azmi when the latter retired in September 2011. In his elevation speech, Tan Sri Arifin Zakaria pledged to continue the transformation of the judiciary, enhance the efficiency of the judiciary and improve the quality of the courts' decisions. True to his words, the Chief Justice recently announced that all superior court judges will be required to declare their assets and reminded the judges to uphold the independence of the Judiciary and to reject interference of any kind.

To improve the quality of the judgements and decisions, the Chief Justice announced that all criminal and civil appeals in the Federal Court will be heard by a 5 member quorum effective from January 2012 while applications seeking leave to appeal will also be heard by the Federal Court's 5 member panel instead of a 3 member panel from March 2012.

This is indeed good news and we at Skrine hope that the transformation will continue and give back to the judiciary the respect it deserves.

From this year onwards, we have introduced a new series, "Landmark Cases", which will feature a discussion on cases that have established new legal principles or have contributed significantly to the development of the law.

We hope that you will enjoy this issue of our newsletter and forget the apocalyptic theories about 2012.

Best Wishes and Thank You.

LEE TATT BOON
Editor-in-Chief
& Senior Partner

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ANNOUNCEMENTS

APPOINTMENT OF NEW PARTNER

We are pleased to announce that Lee Shih has been admitted as a partner of the Firm as of 1 January 2012. We extend our heartiest congratulations to him.

Lee Shih is a member of the Dispute Resolution Division. He is a graduate of the University of Bristol and was called to the Bar of England and Wales.

His primary areas of practice are commercial and corporate litigation with a focus on shareholders disputes and insolvency. He also has a growing international arbitration practice.

ILO AWARDS

The Firm congratulates our Partners, Wong Chee Lin and Siva Kumar Kanagasabai who won the following ILO Client Choice Awards for 2012:

- Wong Chee Lin - Insolvency and Restructuring Practitioner of the Year (Malaysia)
- Siva Kumar Kanagasabai - Employment/Labour Practitioner of the Year (Malaysia)

SKRINE also won the overall Malaysia Country Award.

The awards ceremony took place in London on 22 February 2012 and was attended by both Partners and Senior Partner, Lee Tatt Boon.

LEGAL UP-DATES

The Copyright (Amendment) Bill 2010 which was featured in LEGAL INSIGHTS Issue 3/2011 has come into operation as the Copyright (Amendment) Act 2012 on 1 March 2012.

The decision of the Court of Appeal in *Qimonda Malaysia Sdn Bhd v Sediabena Sdn Bhd & Anor* which was featured in LEGAL INSIGHTS Issue 3/2011 has been reported in [2011] 8 CLJ 269, [2011] MLJU 1204 and [2012] Pt 2 BLR 65

In LEGAL INSIGHTS Issue 4/2011, we featured a write-up on the expedited examination process for trade marks and patents in Malaysia. Since its introduction on 15 February 2011, 223 trade marks applications and 24 patents applications have been received under this expedited process (Source: Bernama News Agency; 19 March 2012).

CLIENTS' FEEDBACK

In an effort to enhance the quality of our legal service for our valued clients, we have created an email address namely: executivecommittee@skrine.com for our clients to provide feedback on matters undertaken by our lawyers. Clients are encouraged to use it to help our lawyers assist you better.

THE END OF

Shannon Rajan provides
Industry Payment and

INTRODUCTION

The Construction Industry Payment and Adjudication Bill 2011 ("CIPA Bill"), which is being presented to the Dewan Rakyat and the Dewan Negara of the Malaysian Parliament during its present session, introduces an interim dispute resolution process, described as 'adjudication', to resolve payment disputes arising from construction contracts and provides remedies for the recovery of payment upon the conclusion of adjudication.

The CIPA Bill is designed to facilitate regular and timely payment in respect of construction contracts with the aim to alleviating cash flow problems that presently plague the construction industry.

WHAT IS ADJUDICATION?

Generally, adjudication is a process that involves a neutral third party, either appointed by the parties to a dispute or by an independent institution, clothed with the authority to make a provisional interim but enforceable decision on disputes referred to him.

The decision of the adjudicator is binding and is to be complied with until and unless the subject matter of the decision is finally resolved by arbitration, litigation or agreement in writing (Section 13), or is otherwise set aside by the Court (Section 15).

STRUCTURE OF THE CIPA BILL

The CIPA Bill is divided into 7 parts:

(a) Part I deals with preliminary matters;

(b) Part II deals with the procedures on the adjudication of payment disputes;

(c) Part III deals with the provisions relating to the adjudicator;

(d) Part IV deals with the enforcement of the adjudicator's decision;

(e) Part V deals with the designation of the adjudication authority;

(f) Part VI deals with the general provisions; and

(g) Part VII deals with the miscellaneous provisions.

PRELIMINARY MATTERS

Section 2 provides that the provisions of the CIPA Bill apply to every construction contract made in writing in relation to construction works carried out wholly or partly within Malaysia, including construction contract entered into by the Government.

A construction contract is defined in Section 4 as a construction work contract or construction consultancy contract. The scope of

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CASH FLOW WOES?

an overview of the Construction Adjudication Bill 2011

'construction work' is wide and includes oil, gas and petrochemical work. Consultancy services include planning and feasibility study, architectural work, engineering, surveying, exterior and interior decoration, landscaping and project management services.

However, the CIPA Bill does not apply to a construction contract entered into by a natural person for any construction works in respect of any building which is less than 4 storeys high and which is wholly intended for his occupation (Section 3).

PAYMENT ISSUES AND PROCEDURES

Any party to a construction contract who claims payment of a sum which has not been paid in whole or in part under a construction contract may serve a payment claim on a non-paying party. 'Payment' is defined by Section 4 of the CIPA Bill to mean *'a payment for work done and services rendered under the express terms of a construction contract'*.

> **"The CIPA Bill is designed to facilitate regular and timely payment in respect of construction contracts"**

The CIPA Bill gives the parties the freedom to agree on the manner of evaluation, frequency and due date of payment but in the absence of such agreement between the parties in the construction contract, the default provisions in Section 36 will apply. Section 35 expressly outlaws *"pay-when-paid"* and other conditional payment provisions in construction contracts and declares such provisions to be null and void.

A brief outline of the adjudication process is set out below.

(a) Upon receipt of a payment claim from the unpaid party, the non-paying party may serve a payment response in writing within 10 working days, disputing the whole or a part of the claim. A non-paying party who does not serve a payment response is deemed to have disputed the entire payment claim (Section 6(4));

(b) After the expiry of the payment response period, the unpaid party or the non-paying party may refer any dispute arising from the payment claim to adjudication by serving a written notice of adjudication (Section 7(2));

(c) Upon the receipt of the notice of adjudication from the unpaid party, an adjudicator may be appointed by agreement of the parties within 10 working days, or failing such agreement, by the Director of the Kuala Lumpur Regional Centre for Arbitration upon request by either or both of the parties (Sections 8(2) and 21);

(d) After an adjudicator is appointed, the claimant is required to serve its written adjudication claim containing the nature and description of the dispute and the remedy sought together with any supporting documents on the respondent and the adjudicator within 10 working days from the receipt of the acceptance of the appointment by the adjudicator (Section 9);

(e) The respondent is then required to serve its written adjudication response within 10 working days from the receipt of the adjudication claim (Section 10). If the respondent fails to serve any adjudication response within the stipulated 10 working days period, the claimant may proceed with the adjudication;

(f) Upon receipt of the adjudication response, the claimant may serve its adjudication reply within 5 working days thereof (Section 11); and

(g) The adjudicator will then be required to decide the dispute and deliver his adjudication decision within 45 working days from the service of the adjudication response or reply, whichever is later, or 45 days from the expiry of the period prescribed for the service of the adjudication response if no adjudication response is received. The prescribed time-frames may be extended by agreement of the parties. If the adjudication decision is not delivered within the prescribed time, that decision will be deemed void (Section 12).

The whole process from the initiation of adjudication process up to the delivery of the adjudicator's decision will take approximately 95 to 100 working days.

THE COURT'S ROLE

Section 15 provides that an aggrieved party may apply to the High Court to set aside an adjudication decision on the ground that (a) the adjudication decision was improperly procured through fraud or bribery, or (b) there was a denial of natural justice, or (c) the adjudicator had not acted independently or impartially, or (d) the adjudicator had acted in excess of his jurisdiction.

Either party may also apply to the High Court for a stay of the adjudication pursuant to Section 16 provided that an application to set aside the adjudication decision has been made, or the subject matter of the adjudication decision is pending final determination by arbitration or the court. The granting of such a stay is within the discretion of the High Court. However, the High Court may, if it sees fit, order the adjudicated amount or part of it

continued on page 13

RESOLUTION OF THE DIRE CONFLICT ON THE PART OF LIQUIDATORS

Lee Shih examines the decision of the Federal Court in Ooi Woon Chee & Anor v Dato' See Teow Chuan & Ors

The Federal Court in *Ooi Woon Chee & Anor v Dato' See Teow Chuan & Ors* [2012] MLJU 9 has reversed the decision made by the Court of Appeal in *Dato' See Teow Chuan & Ors v Ooi Woon Chee & Ors (including Can-One International Sdn Bhd as 15th respondent) and other appeals* [2010] 6 MLJ 459. The Federal Court has clarified several important points of law touching on when a liquidator can be held to be in conflict of interest where the liquidator's accounting firm has provided auditing or other services.

BRIEF FACTS

In 1996, Kian Joo Holdings Sdn Bhd ("Company") had been wound up by the Court by consent of the shareholders. The liquidators of the Company ("Liquidators") were partners of KPMG Peat Marwick ("KPMG") and KPMG Corporate Services Sdn Bhd ("KCSSB") was an entity used by the Liquidators to carry out some of their duties.

The facts leading to the appeal in the Federal Court centred on two main applications filed in the High Court. The first application was filed by the majority contributories ("Majority Contributories") of the Company seeking leave to proceed with legal proceedings ("Leave Application") against the Liquidators, KCSSB, KPMG and Can-One International Sdn Bhd ("Can-One") for alleged misconduct in a tender of the assets of the Company, namely its 34.46% shareholding in Kian Joo Can Factory Berhad ("KJCFB"), and eventual award to Can-One.

The second application was filed by the Liquidators for directions from the High Court as to whether to complete the sale to Can-One ("Directions Application").

At the High Court, the Leave Application was dismissed and pursuant to the Directions Application, the Court directed the completion of the sale to Can-One. The decision of the High Court was reversed by the Court of Appeal. The Liquidators were granted leave to appeal to the Federal Court in respect of both the Leave Application and the Directions Application.

FINDINGS OF THE FEDERAL COURT

The Federal Court first dealt with the issues arising from the Leave Application. The Federal Court noted that the Court of Appeal, when reversing the decision of the High Court, had granted leave to the Majority Contributories to proceed with the suit against the Liquidators where the suit was commenced in the names of the Majority Contributories and not in the name of the Company. The Federal Court held that the High Court was correct in holding that no leave ought to be granted as no cause of action vested in the Majority Contributories. The complaint was that the sale of the Company's shares in KJCFB was improperly conducted and any loss would be suffered by the Company. The proper plaintiff would therefore be the Company and not the Majority Contributories.

Further, the Federal Court agreed that no pecuniary loss was suffered by the Company by accepting Can-One's offer as it was the highest.

The Federal Court then further assessed whether the Majority Contributories had made out a *prima facie* case against the Liquidators in order to allow the Leave Application. The Majority Contributories had raised three main areas in the claim against the Liquidators and the Federal Court looked at each in turn.

Can-One's Offer

The first was the Majority Contributories' claim that Can-One had no valid offer for the Liquidators to accept. The Federal Court analysed the facts surrounding Can-One's offer and held that the Liquidators had correctly exercised their discretion in accepting Can-One's offer.

> **"to constitute actual conflict … there must be another partner from KPMG advising Can-One on the very sale itself in the opposite interest"**

Conflict of Interest

The Federal Court next considered the issue as to whether the Liquidators, KCSSB and KPMG had placed themselves in a position of conflict when the Liquidators accepted the tender from Can-One where Can-One and its holding company were audit clients of KPMG. The Federal Court was guided by the legal principle that there cannot be an actual or apparent conflict on the part of the Liquidators.

In order to constitute actual conflict, the Federal Court held that there must be another partner from KPMG advising Can-One on the very sale itself in the opposite interest. The Federal Court found that there was no one from KPMG or connected with the Liquidators advising Can-One and that KPMG only acted in the audit of Can-One. There was no connection between the sale and the audit and hence, no actual conflict.

On the issue of apparent conflict, the Federal Court assessed the connection between the Liquidators who are partners in KPMG operating out of Kuala Lumpur/Selangor and KPMG's Penang branch who were auditors of Can-One. The Federal Court was of the view that commercial reality was such that large accounting practices will give rise to associations with persons whom insolvency practitioners will sell assets to. To disqualify a liquidator merely because of an audit relationship would mean that almost every large accounting firm would be disqualified from holding a tender exercise.

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The Federal Court held that commercial reality dictated that the existence of such a relationship by itself should not disqualify liquidators or their audit clients. Firstly, there is no express prohibition under the Companies (Winding Up) Rules 1972 for such a disqualification. Secondly, the Federal Court held that the High Court had correctly applied the Canadian case of *Cobrico Development Inc v Tucker Industries Inc* 2000 ABQB 766 ("*Cobrico*") in finding there was no conflict. In *Cobrico*, the appointment of an auction house was criticized because the receiver's firm was the auditor of the auction house in the same way as the Liquidators' firm was the auditor of Can-One. It was held in *Cobrico* that that fact alone did not constitute a conflict of interest.

Alleged Bribe and Solicitation

The Federal Court agreed with the High Court that the allegation of solicitation for a bribe was devoid of merit. The Federal Court examined the chronology of events, in particular how the complaint of improper conduct and fraud were only made by a member of the Majority Contributories after the announcement that Can-One was awarded the sale. The Federal Court also held that the allegation, even if it were true, had no effect on the validity of the agreement with Can-One and whether or not it should be completed. In any event, the Federal Court found that no bribe was ever paid.

There were also other important issues touched on by the Federal Court in relation to other findings made by the Court of Appeal.

Standards Applicable to Liquidators and Judges

The Federal Court examined the Court of Appeal's finding that the Liquidators, as officers of the Court, were expected to abide by the same standards as judges and hence could not hold meetings in connection with a bid outside their offices.

The Federal Court disagreed and held that the standards applicable to a Judge have no application to Liquidators on the sale of assets. The Liquidators do not act in a judicial capacity in selling assets and were instead making business decisions to obtain the best possible price. A liquidator is obliged to enter into the market and to use all powers to get that price. The Federal Court held that it would be unrealistic and against commercial reality to expect a liquidator to sit in his office in the expectation that competitive bids would come streaming in.

Duty Owed by KPMG and KCSSB to the Contributories

The Federal Court held that the Court of Appeal had erred in finding that KPMG and KCSSB owed a fiduciary duty to the contributories of the Company. KPMG and KCSSB were not vehicles used by the Liquidators and thus could not be liable for the alleged acts of the Liquidators. The appointment of the Liquidators was personal and KPMG as a firm of accountants and KCSSB as a company were never appointed as liquidators of the Company. It was held that the Liquidators were perfectly entitled to appoint KCSSB as an agent to assist in the liquidation.

Decision in the Directions Application Not Appealable

At the Court of Appeal, the Liquidators had raised a preliminary objection as to whether the directions given by the High Court were appealable. The question was whether such a direction would fall within the meaning of "*judgment or order of any High Court*" under section 67(1) of the Courts of Judicature Act 1964. While the Court of Appeal held that such directions were appealable, the Federal Court disagreed. It held that the directions given by the High Court were in the nature of advice and were accordingly not a "*judgment or order*" and thereby non-appealable.

COMMENTARY

This Federal Court decision clarifying the issue of conflict of interest on the part of liquidators is welcomed. This decision would similarly apply to the situation where receivers and/or managers ("R&M") are appointed over a company. The mere fact that the accounting firm of a liquidator/R&M has provided any auditing or other services to a company is not sufficient to give rise to a conflict of interest on the part of the liquidator/R&M when dealing with that company. The Federal Court gave great weight to commercial realities and the far-reaching effects of making any finding of conflict of interest.

This decision however may not be the end of this dispute. The Majority Contributories have filed an application to review this decision of the Federal Court on the grounds that the Federal Court grounds of judgment had substantially reproduced the written submissions filed by solicitors for the Liquidators and Can-One in the Federal Court. It has been reported that the Majority Contributories allege that there was insufficient consideration by the Federal Court of the Majority Contributories' case.

It has been further reported that the Liquidators have filed an application to obtain leave to cite the 14 of the respondents and their counsel for contempt of court on the basis that the grounds for their review application showed disrespect to the Court and that the counsel for the 14 respondents may file counter-contempt proceedings against the Liquidators.

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THE NEW KID IN TOWN

Lee Ai Hsian introduces the new form of business entity under the Limited Liability Partnerships Act 2012

The Limited Liability Partnerships Act 2012 ("Act") became law when it was published in the Gazette on 9 February 2012. It is expected to come into operation later this year.

In this first of a two-part article, we will discuss the main features of the Act.

References in this article to a "Part", "Schedule" or "Section" are references to a Part, Schedule or Section respectively of the Act.

FUNDAMENTALS OF A LIMITED LIABILITY PARTNERSHIP

The provisions of the Partnership Act 1961 and the rules of equity and of common law applicable to partnerships do not apply to a limited liability partnership ("LLP") (Section 4).

The key features which distinguish an LLP from a conventional partnership are as follows:

- An LLP is a body corporate and is a separate legal entity from that of its partners (Section 3(1));
- An LLP enjoys perpetual succession (Section 3(2));
- Any change in the partners of an LLP does not affect the existence, rights or liabilities of the LLP (Section 3(3));
- An LLP is capable of suing and being sued, acquiring, owning, holding and developing or disposing of property and doing and suffering such other acts and things as bodies corporate may lawfully do and suffer (Section 3(4));
- An obligation of an LLP, whether arising in contract, tort or otherwise, is solely the obligation of the LLP. A partner remains personally liable in tort for his own wrongful act or omission but is not liable for the wrongful acts or omissions of the other partners of the LLP. The LLP is liable to the same extent as the partner who commits a wrongful act or omission in the course of the LLP's business or with its authority and the liabilities of the LLP are to be borne out of the property of the LLP (Section 21); and
- Every partner is an agent of the LLP and has the power to bind the LLP when the partner is acting within authority and the person with whom the partner is dealing with knows that the partner has authority or that he is a partner of the LLP (Section 23).

FORMATION AND REGISTRATION

General

Section 6 provides that, subject to Sections 7 and 8, two or more persons, whether individuals or bodies corporate, associated for carrying on any lawful business with a view to profit may form an LLP in accordance with the terms of an LLP agreement ("Agreement"). In view of the requirements of Section 6, an LLP may not be formed for a social, recreational or charitable purpose.

Section 13 requires the name of an LLP to end with the expression "Perkongsian Liabiliti Terhad" or the abbreviation "PLT".

Application for registration of an LLP

An application for registration of an LLP must include a statement signed by every person who is to be a partner of the LLP which sets out the particulars specified in Section 10(2), namely:

(a) the name of the proposed LLP;

(b) the general nature of the proposed business of the LLP;

(c) the proposed registered office of the LLP;

(d) the name, nationality and usual place of residence of every proposed partner and where a partner is a body corporate, its corporate name, place of incorporation or origin, registration number and registered office;

(e) the name, nationality and usual place of residence of every person who is to be a compliance officer of the LLP; and

(f) such other information as the Registrar may specify.

> **"Any change in the partners of an LLP does not affect the existence, rights or liabilities of the LLP"**

Notice and certificate of registration of LLP

Upon being satisfied that the requirements for registration under the Act have been complied with, the Registrar will register and allocate a registration number to the LLP as well as issue a notice of registration under Section 11(1)(b). The LLP is deemed to come into existence on and from the date of registration stated in the notice of registration (Section 11(2)).

An LLP may apply to the Registrar for the issue of a "certificate of registration". Although the certificate of registration appears to be a different document from the notice of registration issued under Section 11(1)(b), the Act does not explain the difference between these two documents.

Professional practice partnerships

Section 8 permits an LLP to be formed for the purpose of carrying on a "professional practice". "Professional practice" as defined in the Act is confined to the professions stipulated in the First Schedule, namely chartered accountants, advocates and solicitors and secretaries.

Unlike other forms of an LLP, the partners of a professional

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practice LLP must consist of natural persons who are practising the same profession. Such an LLP must have in force a professional indemnity insurance cover for an amount approved by the Registrar or specified by a governing body of the professional practice, as the case may be.

In addition to the requirements of Section 10(2), an application to register a professional practice LLP is to be accompanied by a letter of approval from the relevant governing body (Section 10(3)).

LLP Agreement

Except as otherwise provided in the Act, the rights and duties of the partners of an LLP as between themselves, and as between the LLP and its partners, are to be governed by the Agreement. In the absence of specific provisions in the Agreement on the matters specified in the Second Schedule, the relevant provisions of the Second Schedule will apply (Section 9(1)).

OTHER OBLIGATIONS AND FEATURES

Some of the other notable obligations and features of an LLP include the following:

(a) *Compliance officer* - An LLP is required to appoint at least 1 compliance officer from amongst its partners or persons who are qualified to act as secretaries under the Companies Act 1965 ("Companies Act"). The responsibilities of a compliance officer are similar to that of a secretary of company. He must be a citizen or permanent resident of Malaysia and ordinarily reside in Malaysia (Section 27);

(b) *Annual declaration* - Every LLP is required to lodge with the Registrar an annual declaration by any 2 of its partners that, in their opinion, the LLP appears or does not appear to be able to pay its debts as they become due in the normal course of business (Section 68);

(c) *Accounts and other records* - Every LLP is required to keep such accounting and other records which will sufficiently explain the transactions and financial position of the LLP as well as give a true and fair view of the state of affairs of the LLP. Such records are to be retained for not less than 7 years. The accounts of an LLP need not be audited unless required under the Agreement (Section 69);

(d) *Carrying on business with less than 2 partners* - If an LLP carries on business with fewer than 2 partners beyond a period of 6 months or such longer period as may be permitted by the Registrar under Section 7(1), a person shall be personally liable, jointly and severally, with the LLP if at the time when the obligation was incurred, that person was a partner of the LLP and knew or ought to have known that the LLP was carrying on business with less than 2 partners beyond the period permitted under Section 7(1) (Section 7(2));

(e) *Receivership and winding-up by the Court* – Subject to the necessary modifications: (i) Part VIII of the Companies Act governs the receivership of an LLP, and (ii) Divisions 2 and 4 of Part X of the Companies Act and the Companies (Winding-up) Rules 1972 apply to the winding-up of an LLP by the Court (Sections 49(1)(a) and 49(1)(b));

(f) *Voluntary winding-up* - The procedures and laws that govern the voluntary winding-up of an LLP are set out in Section 50. An LLP which is unable to pay its creditors is not permitted to initiate a voluntary winding-up unless its creditors waive their claims against the LLP; and

(g) *Foreign LLPs* - Section 44 provides that a foreign LLP may not carry on business in Malaysia unless it is registered as a foreign LLP under the Act. The Third Schedule sets out a list of 10 activities which do not constitute the "carrying on of business." These activities include (i) being a party to legal proceedings, (ii) holding meetings or carrying on other activities concerning its internal affairs, (iii) maintaining a bank account, (iv) effecting any sale through an independent contractor, (v) soliciting or procuring any order which becomes a binding contract only if the order is accepted outside Malaysia, (vi) conducting an isolated transaction that is completed within 31 days, not being one of a number of similar transactions, and (vii) investing its funds or holding property.

CONVERSION

The Act permits a conventional partnership and a private company to convert to an LLP. The procedures for conversion and legal issues that arise from this process will be discussed in the next issue of LEGAL INSIGHTS.

CONCLUSION

The passing of the Act is timely as an LLP provides an alternative form of business entity to a conventional partnership and a company. An LLP provides the benefits of limited liability normally associated with companies whilst allowing its partners the flexibility of adopting an internal structure akin to a conventional partnership.

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AND TWO (OR MORE) SHALL BECOME ONE

Rachel Ng makes a case for incorporation of statutory amalgamations into the Companies Act 1965

Mergers and acquisitions have become a common area of practice for most corporate lawyers these days.

MERGERS IN MALAYSIA

As in most common law jurisdictions, merger and acquisition transactions in Malaysia are usually effected through a shares purchase or an assets purchase. A shares purchase does not achieve full integration as the entities involved remain in existence and continue with their respective businesses.

An assets purchase is a document intensive process which entails, among others, applications for new licences that were held by the seller of the assets, the transfer of employees and of contractual rights and obligations, the latter of which require approval of the affected counter-parties.

Alternatively, a company may undertake a merger through a scheme of arrangement under Section 176 of the Companies Act 1965 ("Companies Act"). As such a scheme is a long-drawn process that requires court sanction as well as the approval of the creditors of the company or business to be acquired, it is usually resorted to only if there are no other practicable means of effecting a merger.

> "several common law jurisdictions have already adopted this form of merger"

MERGERS IN CIVIL LAW JURISDICTIONS

Mergers by operation of law have long since existed in civil law countries such as the Netherlands and Germany.

In essence, such a merger automatically vests the assets and liabilities of the entities in one entity, often described as the surviving entity. The remaining entities will cease to exist upon the merger taking effect.

The most attractive feature of the civil law merger process is the simplicity of the process by which the surviving entity assumes the rights and obligations of the other entities and the seamless manner by which it is achieved.

AMALGAMATIONS IN COMMON LAW JURISDICTIONS

Taking the cue from civil law jurisdictions, several common law jurisdictions have already adopted this form of merger, which we will refer to in this article as "amalgamations".

In 1994, New Zealand amended their Companies Act 1993 No. 105 to facilitate amalgamations whilst Singapore incorporated this procedure into the Singapore Companies Act (Cap 50) in 2006. The Singapore model is based substantially on the New Zealand model.

The Singapore and New Zealand models offer two forms of amalgamation procedures which are free from judicial oversight, namely a "*short form amalgamation*" and a "*long form amalgamation*".

A short form amalgamation may be used when a holding company merges with one or more of its wholly-owned subsidiaries or when two or more wholly-owned subsidiaries of the same holding company merge with each another. The merger of companies that do not satisfy either of the foregoing criteria is effected by a long form amalgamation.

Long form amalgamation

A long form amalgamation is initiated with the preparation of an amalgamation proposal which sets out the detailed terms of the transaction. The board of directors of each amalgamating company is required to pass a resolution to confirm that the amalgamation is in the interest of the relevant company. Each director who votes in favour of the resolution is also required to sign a declaration to confirm that the relevant requirements under the legislation have been satisfied.

The Singapore model goes further to require each director to make a solvency statement in relation to the amalgamating company on whose board he serves.

To protect the rights of the members of the amalgamating companies, the amalgamation proposal and all information that is necessary to assist in the understanding of the nature and impact of the proposed amalgamation must be provided to the members of each amalgamating company. The amalgamation proposal must also be sent to all secured creditors.

The amalgamation proposal must then be approved by a special resolution of members in general meeting of each amalgamating company. Creditors or members may apply to the court for relief in the event that they are being unfairly prejudiced.

Interestingly, the long form amalgamation procedure in New Zealand also confers a right on each member who votes against the amalgamation proposal to be bought-out.

Upon the approval by the members of all the amalgamating companies being obtained, the amalgamation proposal will be lodged with the Registrar of Companies together with the other documents and fees prescribed under the legislation. The Registrar will thereafter issue a notice of amalgamation and, where the amalgamated company is a new company, a notice of incorporation. The amalgamation takes effect from the date stated in the notice of amalgamation and vests all properties, rights, obligations and liabilities of the amalgamating companies in the amalgamated company.

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Short form amalgamation

The procedures for a short form amalgamation are substantially similar to the long form amalgamation. However, it dispenses with certain formal procedures required for a long form amalgamation, such as the requirement for a formal amalgamation proposal.

In Singapore, a short form amalgamation must still be approved by a special resolution of the members of each amalgamating company. A solvency statement must still be made by each director who approves the resolution.

The New Zealand legislation only requires a short form amalgamation to be approved by a board resolution of each amalgamating company. The directors who voted in favour of the resolution are required to sign a certificate stating that the amalgamated company will satisfy the solvency test after the amalgamation.

AMALGAMATIONS IN TAX HAVEN JURISDICTIONS

A codified framework for amalgamations is not new to Malaysia. The amendments to the Labuan Companies Act 1990 ("LCA") that came into force on 11 February 2010 introduced a framework for such amalgamations.

The LCA provides for three forms of amalgamations in Sections 118A, 118B and 118C.

Section 118A allows two or more Labuan companies to amalgamate. This form of amalgamation creates a **new** Labuan entity which must be registered with the Labuan Financial Services and Securities Authority ("LFSA").

The procedures under Section 118A are substantially similar to a Singapore long form amalgamation in that the amalgamating entities are required to prepare an amalgamation proposal and to issue the same to the members and secured creditors of each amalgamating company. The amalgamation proposal is to be approved by special resolution of each amalgamating company. As in the Singapore model, the directors of each amalgamating company are required to make solvency declarations in relation to that amalgamating company.

Section 118C of the LCA provides for a short form amalgamation for amalgamations between a holding company and one or more of its wholly-owned subsidiaries or between two or more wholly-owned subsidiaries of the same corporation.

For short form amalgamations, it is not essential for a new Labuan company to be created. Where the amalgamation involves a holding company, that company must continue as the amalgamated company. In a short form amalgamation of wholly-owned subsidiaries of the same corporation, any of the subsidiaries can be the amalgamated company.

As in Singapore, the LCA requires a short form amalgamation to be approved by special resolution of each of the amalgamating companies.

Certain procedures are dispensed with in a short form amalgamation, thereby reducing the cost and time for effecting such amalgamations. For example, there is no requirement to prepare an amalgamation proposal and the resolutions passed by the amalgamating companies are deemed to be the amalgamation proposal.

For both of the aforementioned forms of amalgamation under the LCA, a certificate issued by the LFSA is conclusive evidence of compliance with all the requirements of the LCA and of the vesting of the assets of the amalgamating companies in the amalgamated company.

Section 118B of the LCA enables a Labuan company to amalgamate with a foreign Labuan company or a corporation provided that the Labuan company continues as the amalgamated company. A foreign Labuan company or corporation is required to obtain all necessary authorisations under the laws of the jurisdiction of its incorporation and to provide the LFSA with documentary proof of such authorisations.

The provisions of Section 118A apply *mutatis mutandis* to an amalgamation under Section 118B. Section 118B is an interesting provision in that it enables cross-border amalgamations to be effected provided that a Labuan company continues as the amalgamated company.

It must be noted that an entity which holds a licence under the Labuan Financial Services and Securities Act 2010 or the Labuan Islamic Financial Services and Securities Act 2010 is not permitted to be involved in any of the three forms of amalgamations under the LCA.

Another tax haven which has recently adopted this court-free procedure into its legal framework is the Cayman Islands. In May 2009, their law was amended to provide for companies to amalgamate by way of merger or consolidation.

CROSS-BORDER AMALGAMATIONS

On 26 October 2005, the European Parliament issued a directive (Directive 2005/56/EC) to facilitate cross-border mergers between limited liability companies that originate from different Member States of the European Union ("EU").

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IF YOU GO TO CAESAR YOU MUST TAKE CAESAR'S JUDGMENT

A commentary on The Government of India v Cairn Energy India Pty Ltd by Janice Tay

The decision of the Federal Court in *The Government of India v Cairn Energy India Pty Ltd & Anor* [2011] 6 MLJ 441 provides authoritative confirmation of the circumstances in which an arbitral award may be set aside under the Arbitration Act 1952 ("1952 Act").

BACKGROUND

Cairn Energy India Pty Ltd ("Cairn") and Ravva Oil (Singapore) Pte Ltd ("Ravva") had entered into a Production Sharing Contract ("Contract") with the Government of India ("GOI"). As disputes arose between the contracting parties concerning the "costs recoveries" and the "calculation of Post Tax Rate of Return ("PTRR") for production sharing purposes", these disputes were referred to arbitration, the chosen seat of arbitration being Malaysia.

The Arbitration

Six issues were referred to and decided by a panel of three Arbitrators ("Arbitral Tribunal"). In the final Award, the Arbitral Tribunal determined four issues in favour of GOI, and the other two, in favour of Cairns and Ravva. Dissatisfied with the determination, the GOI applied to the Malaysian High Court to set aside the Award pursuant to Section 24(2) of the 1952 Act.

The sole issue of challenge raised by GOI pertained to the part of the Award that determined "*the Companies are entitled to include in the accounts, for the purposes of PTRR calculation in accordance with the provisions of Article 16 and Appendix D of the said Contract, sums paid by the Companies in accordance with Article 3.3 of the said Contract*". The challenge was premised on three grounds, namely, that there had been (i) an error of law on the face of the Award, (ii) an excess of jurisdiction, and (iii) misconduct by the majority Arbitrators.

The Decisions of the High Court and Court of Appeal

The learned Judicial Commissioner in the High Court held that there was a manifest error on the face of the Award and set aside that part of the Award.

The High Court's decision was overturned on appeal to the Court of Appeal. Although the judges in the Court of Appeal differed in their grounds for allowing the appeal, their Lordships were unanimous in their view that the learned Judicial Commissioner had erred in his decision warranting the decision to be set aside. The decision of the Court of Appeal was reported at [2010] 2 CLJ 420.

Leave to Appeal to the Federal Court

The Federal Court allowed GOI's application for leave to appeal against the decision of the Court of Appeal on 5 questions of law, 4 of which were raised for the first time before the Federal Court. These 5 questions may be summarised as follows:

(1) Where an award from an international commercial arbitration is submitted for review before the Malaysian Courts under Section 24(2) of the 1952 Act, and the contract provides for the application of one foreign law to govern the contract (namely the laws of India) and another foreign law to govern the arbitration agreement (namely the laws of England), is it proper for the Malaysian Court to apply Malaysian law exclusively to decide the scope of intervention in arbitration awards or the dispute at hand where the seat of arbitration is in Malaysia?

(2) If English law is to apply, whether the appropriate law is that as stated in the English Arbitration Act 1979 which provides for an appeal to the High Court on any question of law arising out of an award?

(3) If Malaysian law is to apply, whether the common law limitation adopted in *Sharikat Pemborong Pertanian dan Perumahan v Federal Land Development Authority* (1971) 2 MLJ 210 ("Sharikat") between a specific reference and general reference in determining the scope of intervention is valid in the light of section 24(2) of the 1952 Act which carries no limitations by itself or where a construction question is involved?

(4) Whether the scope of intervention in arbitration awards is that as stated in *Ganda Edible Oils Sdn Bhd v Transgrain BV (1988)* 1 MLJ 428 ("Ganda Edibile") given that there are conflicting positions presently taken by the Court of Appeal?

(5) Whether the Court of Appeal, as did the Majority Arbitrators before them, failed to appreciate that the paramount rule in the construction of contracts under Indian law is to ascertain the intention of the parties to the bargain and should therefore rely on the wording of the contract as opposed to the commercial sense or industry practice as aids to construction?

> **"the curial law applicable for a challenge to an arbitral award was to be determined in accordance with the chosen seat of arbitration"**

THE DECISION OF THE FEDERAL COURT

In determining the first question, the Federal Court held that the curial law applicable for a challenge to an arbitral award was to be determined in accordance with the chosen seat of arbitration. As the seat of arbitration for this Arbitration was Malaysia, the Malaysian law would be the applicable curial law.

Given the Federal Court's finding that Malaysian law was the applicable curial law, the second question which was premised on the finding that English law would be the applicable law was thus rendered redundant.

With regard to the third question, the Court held the common law distinction adopted in *Sharikat* between a specific reference and general reference in determining the scope of intervention was valid. The Federal Court endorsed the observations made in

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Sharikat and the distinction made between a specific reference and general reference in determining the scope of intervention. The Federal Court said:

"With respect we are not persuaded that we should depart from the long line of authorities holding such a distinction. Where a specific matter is referred to arbitration for consideration, it ought to be respected in that 'no such interference is possible upon the ground that the decision upon the question of law is an erroneous one'. However, if the matter is a general reference, interference may be possible if and when any error appears on the face of the award."

The Court took the view that the question of construction of an agreement referred for determination by the Arbitral Tribunal was a question of law which came within the category of specific reference. Hence, it was not open for any challenge in the broad sense except in the limited circumstances of illegality. In this regard, reference was made to the observation made by the Supreme Court in *Ganda Edible* which stated that an award may be set aside if the decision of the arbitrator was tainted by illegality, such as by deciding on evidence which was not admissible or on principle of construction which the law did not countenance.

As to the fourth question, it was contended that there was conflict between 3 Court of Appeal decisions, 2 of which did not follow *Ganda Edible* while the other did. The Court took the view that the Court of Appeal cases were not in conflict with each other in applying *Ganda Edible* and that they could be read harmoniously. Nevertheless, the Federal Court emphasised that the decision of the Supreme Court in *Ganda Edible* would prevail in the event of any conflict between those Court of Appeal cases.

The Federal Court agreed with the views of the majority of the Court of Appeal on the fifth question, that the issue in question was a specific reference on a question of law. The Court held that as the Appellant could not establish any illegality in the Award, the Court would not intervene. The Federal Court cited with approval, a passage from Scrutton LJ's judgment in *African & East Malaya Ltd v White Palmer & Co Ltd* [1930] 36 Lloyd's LR 113, 114:

"… if you refer a matter expressly to the arbitrator and he makes an error of law you must take the consequences; you have gone to an arbitrator and if the arbitrator whom you choose makes a mistake in law that is your look-out for choosing the wrong arbitrator; if you choose to go to Caesar you must take Caesar's judgment."

Accordingly, the Federal Court dismissed the appeal as the decision of the Arbitral Tribunal on the referenced issue had not been tainted with illegality.

ANALYSIS

The Federal Court has made it expressly clear that if the parties have agreed to refer a specific question of law to an arbitral tribunal for its determination and the arbitral tribunal has done so, the parties must accept the determination by the arbitral tribunal and none of them can thereafter ask the Court to intervene in the Award on error on the face of the award except in the limited circumstances of illegality as set out in *Ganda Edible*.

Although the Federal Court decision was in respect of an application made pursuant to Section 24(2) of the now repealed 1952 Act, it has been held in at least two High Court cases after the introduction of the Arbitration Act 2005 ("2005 Act") that the common law principles relating to challenging an award on the ground that there has been an error on the face of the award would still be applicable under Section 42(1) of the 2005 Act which allows a party to refer to the High Court any question of law arising out of an award.

However, it should be noted that Section 42 falls within Part III of the 2005 Act which *inter alia* provides that the provisions of this Part would apply to domestic arbitrations unless the parties have agreed to opt out of it and would not apply to international arbitrations unless the parties have agreed to apply it.

Nevertheless, the Federal Court's decision on the principles on "error on the face of the award" may be less significant as a result of the recent amendments made to the 2005 Act under the Arbitration (Amendment) Act 2011 ("Amendment Act") which came into effect on 1 July 2011.

The Amendment Act introduced a new Section 42(1A) to the 2005 Act which limits the scope of reference to the High Court to questions of law which substantially affect the rights of one or more of the parties. There has yet to be any reported decision in Malaysia in relation to an application for reference on a question of law under Section 42 of the 2005 Act after the introduction of Section 42(1A). However, it is likely that the application of the common law jurisprudence on error of law on the face of the awards will now be subjected to the criterion that the question of law must be one that substantially affects the rights of one or more of the parties.

The Amendment Act also introduced a new sub-section (4) to Section 51 of the 2005 Act which provides that the 2005 Act will govern all court proceedings relating to arbitration which are commenced after 15 March 2006 notwithstanding that such proceedings arise from arbitration proceedings that were commenced before 15 March 2006. In other words, while arbitration proceedings which were commenced before 15 March 2006 continue to be governed by the 1952 Act, any court proceedings which arise from such arbitration are to be governed by the provisions of 2005 Act and not the 1952 Act.

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LOVE THY NEIGHBOUR

Chan Su-Li tells the tale of the snail in the ginger beer bottle

Imagine this scenario:

You are going through a particularly stressful period. One day, you notice in the mirror that quite a few white hairs have sprouted on your head. You inform your spouse, who quickly heads to a hair care salon and purchases a hair care product for you that, according to the claims on the packaging, will aid in preventing any more white hair growth.

You use the product daily, punctiliously following the instructions printed on the packaging. After a week, you notice that although there do not appear to be any additional white hairs, large clumps of your hair have started to drop-off instead, leaving unsightly bald patches on your head. You file a complaint with the manufacturer of the hair care product and demand for some sort of compensation for the damage you have suffered. However, the manufacturer refuses to acknowledge that your hair loss was caused by their defective product.

What further recourse do you have against the manufacturer? Well, thanks to the celebrated case of *Donoghue v Stevenson* [1932] AC 562, you will be able to make a claim for damages against the manufacturer of the defective product, whether under common law or under a specific consumer law.

> **“ the snail in the ginger beer bottle has defined and shaped the common law tort of negligence ”**

THE FACTS OF THE CASE

It all began on a Sunday evening on 26 August 1928. May Donoghue (“Donoghue”) boarded a tram in Glasgow to Paisley. Upon arrival, Donoghue met with a friend and they proceeded to the Bethany Cafe, owned by a man named Francis Minchella.

Donoghue’s friend ordered from Minchella, and paid for, some refreshment for the both of them. The refreshment consisted of two slabs of ice-cream, each of which was placed in a tumbler, and over which was then poured part of the contents of a bottle of ginger beer.

The ginger beer had been manufactured by David Stevenson (“Stevenson”), and bought from him by Minchella. It was contained in a dark opaque glass bottle. Donoghue drank some of the contents of the tumbler. As her friend then poured the rest of the ginger beer into the tumbler, the remains of a decomposed snail floated out from the bottle.

Donoghue was later diagnosed by her doctor as having suffered from shock and severe gastroenteritis as a result of the nauseating sight of the decomposed snail and in consequence of the impurities in the ginger beer which she had consumed.

Donoghue brought an action against Stevenson, the manufacturer of the ginger beer, claiming £500 as damages for injuries sustained by her through drinking the contaminated ginger beer. By doing so, she sparked off a case that has arguably become one of the most famous cases in English legal history.

THE BASIS OF THE CASE

The foundation to Donoghue’s case was that Stevenson, as the manufacturer of goods intended for consumption and contained in an opaque bottle that prevented inspection, owed a duty to her as a consumer to take care that there was no noxious element in the goods. Donoghue contended that Stevenson should be liable for the damage she suffered as he had neglected such duty.

The common law position at that point in time was that a duty of care was only owed in very specific circumstances, and in an ordinary case, a manufacturer was under no duty to anyone with whom he did not have contractual relations. There were limited exceptions to this rule, one of which was where the goods were dangerous *per se*, and another was where the goods were known by the manufacturer to be dangerous and there had been a deliberate concealment of such a fact, i.e. fraudulent misrepresentation by the manufacturer.

In the case of *Donoghue v Stevenson*, Donoghue could not claim a breach of contract as there was no contractual nexus between Donoghue and the manufacturer, or even the cafe owner, as it was her friend who had ordered and paid for the drink. In addition, ginger beer was not a dangerous product and the manufacturer had not fraudulently misrepresented it. This meant that her case fell outside the scope of the existing cases on product liability.

In the circumstances, Donoghue’s claim was dismissed by the lower court as having no legal basis. However, following an appeal to the House of Lords, the court held, by a majority of three to two, that Stevenson did in fact owe a duty of care to Donoghue, who was the ultimate consumer of the ginger beer.

THE NEIGHBOUR PRINCIPLE

Lord Atkin delivered the leading judgement, whereby he explained the “neighbour principle” which was based on a teaching in the Bible that one should “love thy neighbour”. According to Lord Atkin:

“The rule that you are to love your neighbour becomes in law, you must not injure your neighbour; and the lawyer’s question, ‘Who is my neighbour?’ receives a restricted reply. You must take reasonable care to avoid acts or omissions which you can reasonably foresee would be likely to injure your neighbour. Who, then, in law is my neighbour? The answer seems to be - persons who are so closely and directly affected by my act that I ought reasonably to have them in contemplation as being so affected when I am directing my mind to the acts or omissions which are called in question.”

His Lordship then stated that:

“... a manufacturer of products, which he sells in such a form as to show that he intends them to reach the ultimate consumer in the form in which they left him with no reasonable possibility of intermediate examination, and with knowledge that the absence

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of reasonable care in the preparation or putting up of products will result in an injury to the consumer's life or property, owes a duty to the consumer to take that reasonable care."

Applying the above principles, the learned Judge held that as the ginger beer was contained in an opaque bottle and could not be inspected before being consumed, Stevenson owed a duty of care to Donoghue as it was reasonably foreseeable that Donoghue would suffer injury if he failed to exercise reasonable care in the manufacture of the ginger beer.

The House of Lords then remitted the case back to the trial court for further determination. The case did not proceed to trial and was settled by the executors of Stevenson's estate after his demise.

SIGNIFICANCE OF THE DECISION

The majority decision of the House of Lords in *Donoghue v Stevenson* is a significant landmark in the English common law. Firstly, it established negligence as a distinct tort. Secondly, it also established that the absence of privity between the litigants did not preclude liability in tort.

Donoghue v Stevenson also established that the manufacturer of a product owes a duty of care to the ultimate consumer or user. Last but not the least, it established that the criterion for the existence of a duty in the law of negligence is whether the defendant ought reasonably to have foreseen that his acts or omissions would likely result in damage or injury to the plaintiff.

The case is also important to the development of consumer law. The legal position that manufacturers owe a duty of care to the end consumers, even in the absence of any contractual relationship, forms the basis of many consumer protection laws, such as the Consumer Protection Act 1999.

The "neighbour principle" has been further refined by the courts in various negligence cases that have followed suit. A number of other factors have now to be considered before a finding of negligence can be made. These include whether the damage was foreseeable, the proximity of the relationship between the parties, and whether it is just in the circumstances to impose a duty of care.

The case of the snail in the ginger beer bottle has defined and shaped the common law tort of negligence. Although it has been modified by subsequent case law and statutes, its influence can still be felt to this very day.

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THE END OF CASH FLOW WOES?

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to be deposited with the Director of the Kuala Lumpur Regional Centre for Arbitration.

ENFORCEMENT OF THE ADJUDICATION DECISION

Section 28 provides that a party may apply to the High Court to enforce an adjudication decision as if it is a judgment of the Court.

A party may suspend performance or reduce the rate of progress of performance of any work or services under a construction contract if the adjudicated amount pursuant to the adjudication decision has not been settled by the other party (Section 29).

GAZING INTO THE CRYSTAL BALL

The CIPA Bill was introduced to protect the subcontractors in the construction industry by ensuring regular and timely payments of progress claims to them and providing speedy resolution of disputes.

> **"a party may ... enforce an adjudication decision as if it is a judgment of the Court"**

Sceptics have argued that statutory adjudication is superfluous as the same objective can be achieved through the expedited arbitration process.

The statistics from other jurisdictions which have adopted statutory adjudication, such as the United Kingdom and Singapore, have revealed that stakeholders in the construction industry would generally accept the adjudication decisions, and would not pursue the matter further either in court or in arbitration. As a result, the number of litigation and arbitration proceedings relating to construction disputes have been substantially reduced since the introduction of statutory adjudication.

If statutory adjudication under the CIPA Bill receives a similar level of receptiveness in Malaysia, then construction-related litigation and arbitration proceedings will similarly be reduced. Perhaps the CIPA Bill will achieve its objective of ending the cash flow woes of subcontractors in the Malaysian construction industry.

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HANDS OFF THE ROYAL COMMISSION!

Wai Loon examines the Federal Court's decision in Royal Commission of Enquiry v Tun Dato' Seri Ahmad Fairuz

FACTS OF THE CASE

The decision of the Federal Court in *Members of the Royal Commission of Enquiry v Tun Dato' Seri Ahmad Fairuz bin Dato' Sheikh Abdul Halim* [2011] 6 MLJ 490 concerns a person's right to challenge in a court of law the findings made by a Commission of Enquiry that was set up to investigate, determine and make recommendations in relation to certain matters that arose from a video clip that contained controversial material connected with the Malaysian judiciary ("Video Clip").

The Video Clip contained images of a man engaged in a telephone conversation relating to the appointment of judges. The Video Clip went viral after it first surfaced on the internet on 19 September 2007, and led to furious debates that questioned the independence of the Malaysian judiciary.

The Government of Malaysia ("Government") took immediate steps to set up an independent panel to investigate into the authenticity of the Video Clip. On the recommendation of the panel, the Government requested His Majesty the Yang di-Pertuan Agong to establish a Commission of Enquiry.

> **" the findings of the Commission were not 'decisions' within the ambit of O. 53 r. 2(4) RHC "**

On 12 December 2007, a Commission of Enquiry ("Commission") was set up pursuant to section 2 of the Commissions of Enquiry Act, 1950 ("Act"). The terms of reference to the Commission included the following:

- to enquire into the authenticity of the Video Clip;
- to identify the person speaking on the telephone, the person he was speaking to as well as those mentioned in the telephone conversation;
- to enquire into the truth or otherwise of the content of the telephone conversation in the Video Clip;
- to determine whether any misbehaviour had been committed by the persons identified or mentioned in the Video Clip; and
- to recommend appropriate action, if any, to be taken against the persons identified or mentioned in the Video Clip.

After a month long hearing, the Commission completed and submitted its report to the Yang di-Pertuan Agong ("Report") containing the findings and recommendations, *inter alia*, as follows:

- The Video Clip was authentic;
- Certain individuals depicted or mentioned in the Video Clip were identified and named in the Report;
- The content of the conversation in the Video Clip was true in substance and in material particulars;
- There was sufficient evidence of misbehaviour on the part of certain individuals mentioned or identified in the Video Clip; and
- There was sufficient cause to invoke various laws, such as the Penal Code and the Legal Profession Act, 1976, against certain individuals mentioned in the Video Clip.

Having made such findings, the Commission recorded that it was up to the Attorney General of Malaysia ("AG") and the Bar Council of Malaysia to take appropriate actions against the individuals implicated in the Report. The Report was transmitted to the Government who made the Report available to the public.

On or about 22 October 2009, it was reported in the media that the AG decided that no further action needed to be taken arising from the findings made in the Report.

THE APPLICATIONS BY THE RESPONDENTS

After the release of the Report to the public, three individuals who were implicated in the Report ("respondents") filed separate applications for leave for an order of *certiorari* to quash the findings of the Commission pursuant to Order 53 ("O. 53") of the Rules of the High Court, 1980 ("RHC").

In support of their applications, the respondents alleged that the findings of the Commission were tainted due to bias and prejudice and were contrary to the principle of law.

The respondents also contended that paragraph 1 of the Schedule to the Courts of Judicature Act, 1964 ("CJA") gave the court wide powers to issue an order of *certiorari* and that O. 53 r. 2(4) ("O. 53 r. 2(4)") of the RHC which limits such right to a 'decision' of a public authority was *ultra vires*.

The AG objected to the applications by the respondents and argued that the findings of the Commission were not 'decisions' within the ambit of O. 53 r. 2(4). The AG also contended that the respondents could not be construed as persons 'adversely affected' by the Commission's findings.

DECISIONS OF THE HIGH COURT AND THE COURT OF APPEAL

The High Court upheld the objections by the AG and dismissed the respondents' applications.

The respondents appealed. The Court of Appeal, by a majority decision of 2 - 1, allowed the respondents' appeals.

The AG obtained leave to appeal to the Federal Court.

THE DECISION OF THE FEDERAL COURT

The sole question cited for determination by the Federal Court was whether the findings of the Commission are reviewable under

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O. 53 of the RHC.

As a starting principle the Federal Court stated that O. 53 permits a person who is adversely affected by the decision of a public authority to make an application for a judicial review of that decision. The person must however obtain leave before his substantive motion can be heard.

The Federal Court answered the question cited to it in the negative on 2 grounds. Firstly, the findings of the Commission were not 'decisions' within the ambit of O. 53 r. 2(4) RHC, and the respondents could not be construed as persons "adversely affected" by the findings of the Commission, and hence, O.53 RHC did not apply in such a situation. Secondly, it would be against public policy to allow the findings of the Commission to be challenged in the courts.

Do findings of the Commission come within the ambit of O. 53 RHC?

According to Raus FCJ, it is trite law that the purpose of an order for *certiorari* is to quash the legal effect of a decision. His Lordship adopted the principles laid down in *Council of Civil Service Unions and others v Minister for the Civil Service* [1984] 3 All ER 935 where the House of Lords held that for a decision to be susceptible to the court's reviewing powers, there must first be a decision by a decision maker or a refusal by him to make a decision, and that decision must affect the aggrieved party by either altering his rights or obligations or depriving him of the benefits which he has been permitted to enjoy.

The Federal Court held that although the Commission was a public authority, it was not a decision making body. According to Raus FCJ, a closer look at the Report revealed that the Commission did not make legal decisions. The Report consisted of findings and recommendations of the Commission on the terms of reference entrusted upon them. Being mere findings and recommendations it did not bind the respondents, not even the Government.

The learned Federal Court Judge acknowledged that, notwithstanding that the Commission had made strong findings that there was sufficient cause to invoke various laws against certain individuals mentioned in the Video Clip, including the respondents, such findings remained mere findings. The Court concluded that such findings were not reviewable as the respondents' legal rights were not directly affected by the findings nor had they been deprived of any benefit which they had been permitted to enjoy.

Accordingly, the Court agreed with the minority decision of the Court of Appeal and held that the findings and recommendations of the Commission did not come within the ambit of O. 53 of the RHC.

The Federal Court also agreed with the minority decision of the Court of Appeal that there was no inconsistency between O. 53 r. 2(4) and paragraph 1 of the Schedule to the CJA. According to His Lordship, the word 'decision' in O. 53 r. 2(4) did not run foul of paragraph 1 of the Schedule to the CJA and was not *ultra vires*.

Public interest

The Federal Court was of the view that there was a strong policy consideration against allowing the findings of the Commission to be challenged in the courts. If such proceedings were allowed to be challenged either at the onset or during its continuance by prohibition or at its conclusion, by *certiorari*, its purpose would come to naught and make the setting up of a Commission a meaningless exercise and a waste of public funds.

Hence, the Federal Court concluded that it would be against public policy to subject the findings and recommendations of the Commission to judicial review. In coming to this conclusion, the Federal Court declined to follow the position taken by the New Zealand Court of Appeal in *Re Erebus Royal Commission; Air New Zealand Ltd v Mahon (No.2)* [1981] 1 NZLR 618, which held that the findings of a Royal Commission were amenable to judicial review. According to the apex court, this policy consideration was the more important reason for its decision.

There was also a related, but non-legal, reason for the decision in this case. At the heart of the inquiry into the Video Clip was the image and independence of the Malaysian judiciary. It was because of this that the Commission was set up to investigate and make recommendations for the betterment of the judiciary. The Federal Court opined that therefore, it would not make any sense if the findings of the Commission were now allowed to be reviewed by those courts.

SIGNIFICANCE OF THE DECISION

This decision of the Federal Court has put to rest any confusion caused by the different opinions of the majority decision and the dissenting judgment of the Court of Appeal.

This decision of the apex court of Malaysia is significant as it makes it unmistakably clear that findings and recommendations of Commissions of Enquiry set up under the Act are not amenable to judicial review.

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GREAT EXPECTATIONS

Trishelea Sandosam explains Malaysia's landmark gender discrimination case

INTRODUCTION

In July 2011, the High Court delivered a landmark decision in *Noorfadilla binti Ahmad Saikin v Chayed bin Basirun and Ors* [2012] 1 CLJ 769 when it held that refusal to employ a woman on the grounds of pregnancy alone is a form of gender discrimination, and thus unconstitutional under Article 8 of the Federal Constitution.

This well-reasoned and truly significant judgment, which expounds the concept of gender discrimination as defined under the Convention on the Elimination of All Forms of Discrimination against Women ("CEDAW") has received wide praise from the legal community and non-governmental organisations and has been nominated for the 2012 International Gender Justice Uncovered Award.

This article explains the salient points of this judgment, which has far-reaching effects on women in Malaysia.

BACKGROUND FACTS

Noorfadilla binti Ahmad Saikin ("the Plaintiff") applied to the Hulu Langat District Education Office for the post of an untrained relief teacher ("GSTT") pursuant to a circular ("Circular") from the Ministry of Education ("Ministry"). The Plaintiff attended an interview where she was asked questions of a general nature. At no point before or during the interview was she asked whether she was pregnant.

Several days after the interview, the Plaintiff received confirmation that her application had been successful. When she attended the Hulu Langat office as instructed, she was briefed on the terms of employment and was asked to report for duty immediately. During this time, an officer enquired if she was pregnant. The Plaintiff indicated that she was and, as a result, the post offered to her was revoked.

The Plaintiff wrote to the Ministry several times to seek an explanation. The Ministry responded and stated that a pregnant woman cannot be employed to the post of GSTT for the following reasons: (i) the duration of time between delivery and recovery to full health is lengthy; (ii) a pregnant woman may be unable to attend to her job frequently due to various health reasons; (iii) she would need to be replaced by a new teacher, who would require further briefings; and (iv) the GSTT post cannot be filled by "replacement" teachers.

The Ministry added that the purpose of employing GSTT was to overcome the shortage of teachers, not to add to the problem.

The Plaintiff's solicitors wrote to the defendants demanding restoration of her employment, but to no avail. Undeterred, the Plaintiff commenced legal proceedings where she named two district officers, the Selangor Education Department State Director, the Chief Director of the Ministry, the Minister and the Government of Malaysia as defendants in the action ("Defendants"). The Plaintiff sought a declaration that she was qualified and entitled to be appointed as a GSTT and that the Defendants' withdrawal of her appointment as a GSTT was unlawful, unconstitutional and void.

ISSUE

The main issue before the High Court was whether the action or directive of the Defendants in refusing to allow a pregnant woman to be employed was tantamount to gender discrimination and in violation of Article 8(2) of the Federal Constitution.

Before discussing the judgment, a brief overview of CEDAW is set out below to enable greater appreciation and understanding of the judgment.

CEDAW

CEDAW was adopted in 1979 by the United Nations General Assembly and is the foremost United Nations treaty on women's rights. It consists of 30 articles. Malaysia acceded to the Convention on 5 July 1995.

> **" Pregnancy is a form of gender discrimination because of the basic biological fact that only women have the capacity to become pregnant "**

Article 1 of CEDAW defines discrimination against women as *"any distinction, exclusion or restriction made on the basis of sex which has the effect or purpose of impairing or nullifying the recognition, enjoyment or exercise by women, irrespective of their marital status, on a basis of equality of men and women, of human rights and fundamental freedoms in the political, economic, social, cultural, civil or any other field."*

Article 11(1)(b) of CEDAW provides that *"State Parties shall take all appropriate measures to eliminate discrimination against women in the field of employment in order to ensure, on a basis of equality of men and women, the same rights, in particular ... the right to the same employment opportunities, including the application of the same criteria for selection in matters of employment."*

Article 11(2)(a) requires States Parties to take appropriate measures to prohibit dismissal on the grounds of pregnancy.

The word 'gender' was inserted into Article 8(2) of the Federal Constitution in 2001 in order to comply with Malaysia's obligation under CEDAW. It now reads as follows: *"... there shall be no discrimination against citizens on the ground only of religion, race, descent, place of birth or gender in any law or in the appointment to any office or employment under a public authority ..."*

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DECISION OF THE HIGH COURT

CEDAW and gender discrimination

The learned Judge, Dato' Zaleha binti Yusof J, opined that the Court had *"no choice"* but to refer to CEDAW in clarifying the term 'equality' and the concept of gender discrimination under Article 8(2) of the Federal Constitution. Relying on *Mohd Ezam Mohd Noor v Ketua Polis Negara* [2002] 4 MLJ 449, the Court held that as CEDAW is a convention and not a mere declaration, it has the force of law and is binding on member states.

The Court noted its duty to take into account the government's obligation under CEDAW in interpreting Article 8(2) of the Federal Constitution. Her Ladyship also drew inspiration from Australian and Indian jurisprudence which advocates the use of international conventions and obligations in the construction of domestic legislation.

The Judge also referred to several instances where Malaysia had expressed its commitment to ensuring that the principles enunciated under CEDAW were given full effect under Malaysian law. For example, during the Putrajaya Declaration and Programme of Action on the Advancement of Women in Member Countries of the Non-Aligned Movement, Malaysia had pledged to take all necessary measures in the area of law and policy to eliminate discrimination against women in the public and private sector and to eliminate impediments to women's equality.

Her Ladyship also referred to the judicial colloquium on the Domestic Application of International Human Rights Norms in India in 1998, attended by the then Chief Justice of Malaysia, which concluded with a statement by the Convener that national courts are to have regard to international obligations which a country undertakes, even if those obligations have not been incorporated into domestic law.

In applying Article 1 and 11 of CEDAW, and drawing inspiration from the Canadian Supreme Court case of *Brooks v Canada Safeway Ltd* [1989] 59 DLR (4th) 321, the learned Judge held that pregnancy is a form of gender discrimination because of the basic biological fact that only women have the capacity to become pregnant.

Rejection of the Defendants' arguments

The Defendants averred that the decision not to employ a pregnant woman for the GSTT post was a policy consideration

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AND TWO (OR MORE) SHALL BECOME ONE

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The merging companies are required to draw-up common draft terms that contain prescribed information. The common draft terms provide information of the transaction to enable members to make an informed decision on the proposed merger. These terms are published at least one month before the date of the general meeting of the merging companies to decide on the merger.

An independent expert report is to be issued to the members of the merging companies at least one month before the general meeting to assist them to make an informed decision at the respective general meetings.

Finally, the laws of the EU Member State country in which the merged entity will exist apply to effect the merger. A pre-merger certificate has to be granted by a designated court of each Member State to scrutinise the legality of the cross-border merger. This certificate will conclusively attest to the proper completion of the pre-merger acts and formalities.

The directive also provides for a simplified process where the merger is carried out by a company which holds all the shares of the target company.

CONCLUSION

As it can be seen from the above, the codified procedures for amalgamations simplify the amalgamation process.

In the Review of the Companies Act 1965 Final Report, the Corporate Law Reform Committee had recommended that extensive reforms be made to the Companies Act. However, the Committee did not make any recommendation that a statutory framework be adopted in relation to amalgamations.

As mergers and acquisitions are a daily occurrence in the Malaysian corporate sector, it is proposed that the Government should introduce a statutory framework for amalgamations in the forthcoming amendments to the Companies Act. This will not be a ground-breaking move as this framework already exists in the LCA.

As cross-border mergers and acquisitions are becoming more common these days, it may one day be appropriate for ASEAN to adopt a cross-border amalgamation framework that is similar to the EU's Directive 2005/56/EC.

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TURNING A BLIND EYE

A commentary on MPI Polyester Industries Sdn Bhd v Eng Koo Kiang & Ors [2011] 8 CLJ 236 by Siva Kumar Kanagasabai

THE FACTS

The facts, as elicited from the testimony of witnesses and documents produced at the trial, are set out below.

The Plaintiff carried on the business of the manufacture and sale of polyester resins.

The defendants are the former General Manager, Marketing Manager, Logistics Executive and Plant Manager respectively of the Plaintiff ("Defendants").

Despite the rising prices of the Plaintiff's products at the material time, the Plaintiff experienced low profit margins. The Plaintiff then commenced an internal audit in early 2003 to investigate into the matter.

The internal audit disclosed that the 2nd Defendant had procured the Plaintiff to sell its products to non-existent companies, companies owned by relatives of the 2nd Defendant or by way of dubious contracts at low prices. The products were on-sold by the purported purchasers for higher sums, thereby enriching the 2nd Defendant.

The Plaintiff also produced evidence that the 1st Defendant had wrongfully and in breach of his contract of service, caused the Plaintiff to sell its products to a company where the contact person was the 1st Defendant's son at a price which was lower than the Plaintiff's actual average export price for the products.

During the trial, the Plaintiff also produced 10 personal registers and 16 cheque butts that had been seized from the 2nd Defendant. These documents disclosed that the 1st Defendant had received RM170,760, the 3rd Defendant RM8,950 and 4th Defendants RM178,827 from the 2nd Defendant.

Arising from the findings of the internal audit, the Plaintiff terminated the employment of the 1st to 3rd Defendants in July 2003. The 4th Defendant resigned in February 2003.

THE HIGH COURT PROCEEDINGS

The Plaintiff brought a claim against the Defendants on the premise that the Defendants had wrongfully and/or maliciously conspired amongst themselves to defraud and injure the Plaintiff in its business.

The Plaintiff also alleged negligence and breach of fiduciary duty against the 1st and 4th Defendants and sought an account of secret profits or commission by the 1st and 4th Defendants.

The 2nd Defendant chose not to defend the claim after filing his defence and judgment was entered against him before the trial. The 3rd Defendant entered into a consent judgment a day before trial.

The 1st and 4th Defendants, in their defence, asserted that they had no knowledge of the 2nd Defendant's actions. They also contended that the payments received from the 2nd Defendant were loans made to them.

The High Court allowed the Plaintiff's claim and ordered the 1st and 4th Defendants to pay various sums to the Plaintiff.

The following were among the issues that were considered by the learned Judicial Commissioner, Harmindar Singh Dhaliwal, in his judgment.

Negligence by the 1st Defendant as the General Manager

The Court held that it was undeniable that the 1st Defendant, as a general manager who had overall control of the operations and assets of the Plaintiff, owed a duty to the Plaintiff to exercise reasonable diligence to ensure that there were no losses and certainly no profits made by the employees at the expense of the Plaintiff.

> **"the 1st Defendant ... owed a duty to the Plaintiff to exercise reasonable diligence to ensure that there were ... no profits made by the employees at the expense of the Plaintiff"**

The learned Judicial Commissioner was satisfied that on the facts of the case, the 1st Defendant had knowledge of, and was complicit with, the actions of the 2nd Defendant. Accordingly, the Court held that it was patently obvious that the 1st Defendant had breached his duty.

Breach of fiduciary duty by the 1st and 4th Defendants

The learned Judicial Commissioner cited various authorities, including *Clerk & Lindsell on Torts* and *Bristol v West Building Society v Mothew* [1996] 4 All ER 698, as authority for the proposition that a breach of fiduciary duty is a civil cause of action for a failure to meet one of the obligations that, in equity, had created a special relationship of fiduciary and principal, which if established would entitle the principal to equitable compensation for his loss or to restitution for the fiduciary's unauthorized gain.

From the nature of the functions and duties the 1st and 4th Defendants, the Court had no doubt that both these Defendants owed fiduciary duties to act in good faith and of loyalty and fidelity to the Plaintiff. These duties precluded the Defendants from acting in a manner whereby their duty and interest may conflict and from acting for their own benefit to the detriment of their employer without their employer's consent.

SIVA KUMAR KANAGASABAI

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Based on the evidence presented, the Court held that both the 1st and 4th Defendants had clearly breached their fiduciary duty by acting in a manner which enriched themselves at the expense of the Plaintiff.

Conspiracy to injure the Plaintiff's business

In determining the issue of conspiracy, the Court identified and restated the law governing the 2 forms of the tort of conspiracy, namely 'conspiracy to use unlawful means' and 'conspiracy to injure'. 'Conspiracy to use unlawful means' is proven when 2 or more individuals combine to commit an unlawful act or to effect an unlawful purpose with the intention of causing injury or damage to the plaintiff.

In the case of 'conspiracy to injure', lawful means are used but the plaintiff must prove that there was a predominant purpose on the part of the defendants to injure the plaintiff in carrying out their common purpose.

Although the Plaintiff had used the phrase 'conspiracy to injure', the Court held that the Plaintiff had argued its case on the basis of 'conspiracy to use unlawful means'. Hence in essence, all that the Plaintiff had to prove was that the Defendants had the intention to injure the Plaintiff and that it was not necessary to prove that it was the predominant motive. According to the Court, it was clear in the present case that the Defendants had used unlawful means to carry out their illegitimate activities by the manner in which they had acted to procure secret profits for themselves.

The learned Judicial Commissioner held that conspiracy involved an agreement to work on the furtherance of a common purpose. As there was clear evidence of knowledge and complicity on the part of the Defendants of the transactions that enriched them to the detriment of the Plaintiff, the Court was more than satisfied that the Plaintiff had succeeded in establishing that the Defendants had committed conspiracy.

Whether 1st and 4th Defendants received secret profits from the 2nd Defendant

The Court rejected the contention by the 1st and 4th Defendants that the payments received from the 2nd Defendant were loans. On the evidence of the cheque butts, the 1st Defendant's personal registers and the evidence of the 3rd Defendant, the Court was satisfied that the payments were in fact secret profits or commissions received by the 1st and 4th Defendants.

COMMENTARY

Given the strong evidence produced to the Court that the Defendants had conspired and participated in a scheme to earn secret profits for themselves to the detriment of the Plaintiff and that the 1st and 4th Defendants had received a part of such secret profits from the 2nd Defendant, it was foregone that the Court would award judgment in favour of the Plaintiff.

Nevertheless this case is interesting as the learned Judicial Commissioner had imposed a duty on the 1st Defendant, as the general manager who had overall control of the operations and assets of the Plaintiff, to exercise reasonable diligence to ensure that no profits were made by the employees at the expense of the Plaintiff and not just plead ignorance. This proposition is consistent with the duty of an employee to report the wrongdoings of his fellow employees even where the wrongdoing is committed by his superior. In *Swain v West (Butchers) Ltd* [1936] 3 All ER 261, Greene LJ put it as follows:

"The Plaintiff was responsible for the management of the business and was responsible for seeing that the business was conducted honestly and efficiently by all who came under his control. If the dishonesty of a fellow servant came within his notice he should tell the board ... The plaintiff's duty was to report to his employer that the managing director had endeavoured to persuade him to do something which was dishonest and which would, if carried out, be a breach of his duties in controlling the business of the company."

This proposition was applied by the Malaysian Industrial Court in *Mohamad Aminuddin Md Zain & Anor v Perbadanan Usahawan Nasional Berhad* [2006] 3 ILR 2172. In that case, the Company Secretary and the Legal Advisor were dismissed *inter alia* for committing misconduct in not reporting to the board of directors the instructions from their superior, the Chief Executive Officer, to participate in the issuance of a bond on behalf of the employer without the knowledge of the board. The Industrial Court found their dismissal to be justified.

It can be seen from the above that employees, management staff in particular, have to be vigilant and when they become aware of the wrongdoings of their fellow employees, whether subordinate or superior, they have a duty to report it to their employer and not just turn a blind eye.

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A TALE OF TWO TAX CASES

Sarah Kate Lee examines two recent cases on the deductibility of sales incentives

The issue as to whether sales incentives commonly paid to marketing agents and dealers are fully deductible expenses or are to be treated as entertainment expenses that are subject to separate deductibility rules was considered recently by the Courts in *NV Alliance Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri* [2012] 1 MLJ 441 ("NV Alliance Case") and *Ketua Pengarah Hasil Dalam Negeri v Khind-Mistral (Borneo) Sdn Bhd and another appeal* [Tax Appeal: KCH-14-2-2011] ("Khind Case").

DEDUCTIBILITY AND ENTERTAINMENT EXPENSES

As a general rule, section 33(1) of the Income Tax Act 1967 ("Act") allows an expense that is wholly and exclusively incurred in the production of gross income to be deducted against gross income when computing taxable income.

On the other hand, an entertainment expense is currently only allowed a 50% deduction against gross income under section 39(1)(l) of the Act unless it is specifically allowed for full deduction under any of the 8 provisos contained in section 39(1)(l).

> **" the cash incentive expenses clearly could not come within the meaning of the words 'or hospitality of any kind' "**

The word "entertainment" is defined in section 18 of the Act to include:

"*(a) the provision of food, drink, recreation or hospitality of any kind; or*

(b) the provision of accommodation or travel in connection with or for the purpose of facilitating entertainment of the kind mentioned in paragraph (a),

by a person or an employee of his in connection with a trade or business carried on by that person."

THE NV ALLIANCE CASE

Background Facts

NV Alliance Sdn Bhd ("NV") carries on the business of marketing burial plots, urn compartments and funeral packages. In the course of its business, NV appointed marketing agents who were paid commissions for their work.

To motivate the agents to increase sales, NV introduced incentive schemes whereby the agents who achieved certain set sales targets were paid various types of incentives including cash incentives. These payments were claimed by NV as deductions against its gross income under section 33(1) of the Act.

The Inland Revenue Board ("IRB") disallowed the deductions on the ground that such expenses were "entertainment" expenses under section 39(1)(l) of the Act which at the relevant time, did not allow such expenses to be deducted.

The Special Commissioners of Income Tax ("Commissioners") however ruled that the expenses were related to the performance of profit earning operations as they were wholly and exclusively incurred in the production of NV's gross income pursuant to section 33(1) of the Act and were not disallowed deductions by virtue of section 39(1)(l) of the Act.

On appeal, the High Court overturned the decision of the Commissioners and agreed with the IRB that the incentives were caught under the definition of "entertainment" in section 18 of the Act and therefore were not deductible under section 39(1)(l) of the Act.

NV appealed to the Court of Appeal against the decision of the High Court.

Decision of the Court of Appeal

The Court of Appeal set aside the Order of the High Court and restored the Deciding Order of the Commissioners by holding that the cash incentive payments were not "hospitality" expenses, and hence, were not entertainment expenses under section 39(1)(l) of the Act. Thus, NV was entitled to the deductions claimed in respect of the cash incentive payments.

In arriving at its decision the Court of Appeal held that the *noscitur a sociis* rule of statutory interpretation was applicable and that the more general words '*or hospitality of any kind*' in section 18(a) of the Act must be restricted to a sense analogous to that of the less general words, namely, '*food, drink, recreation*'.

The Appellate Court held further that in determining as to whether or not the cash incentive expenses came within the meaning of '*or hospitality of any kind*', it was necessary to take into account the words preceding that phrase, that is to say, the words '*food, drink, recreation*'.

The Court concluded that the cash incentive expenses clearly could not come within the meaning of the words '*or hospitality of any kind*' if the meaning to be given to the words '*or hospitality of any kind*' is limited accordingly.

The Court went on to state that it would arrive at the same conclusion even if it were to apply the *ejusdem generis* rule where the meaning to be given to the general words '*or hospitality of any kind*' in section 18(a) must be restricted to the same genus as '*food, drink, recreation*'.

The Court then concluded that if the meaning to the expression,

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'*or hospitality of any kind*' is so confined, it would then clearly exclude the cash incentive payments.

THE KHIND CASE

Background Facts

Khind-Mistral (Borneo) Sdn Bhd ("KM") carries on the business of dealing and trading in electrical products under the brand name 'Khind'.

KM appointed dealers to sell their products and in 1996 introduced a scheme to motivate and reward dealers who reached their sales target by giving them trips to the local factory and tourist destinations both local and abroad.

These incentives were in addition to the commissions and discounts given to the dealers. For the years of assessment 2000, 2002 and 2003, KM deducted all the expenses for these trips from their gross income when declaring their taxable income under section 33(1) of the Act.

The IRB took the position that these expenses were in fact entertainment under section 18 of the Act and not allowed under section 39(1)(l).

> **" the 'business promotion' aspect of the activity was the material consideration "**

The Commissioners ruled that the incentive trips were expenses deductible under section 33(1) of the Act. The Commissioners also decided that the IRB could not impose a penalty as KM had clearly and correctly described the expenses in the return forms and made full disclosure to the IRB.

Both parties then appealed and cross-appealed to the High Court.

Decision of the High Court

The High Court laid down the principles of statutory interpretation by holding that where the sections are plain and unambiguous, the Court must give effect to the natural and ordinary meaning of words and when interpreting a tax law, the interpretation must be strict.

The High Court then referred to the Court of Appeal decision of *Aspac Lubricants (Malaysia) Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri* [2007] 5 CLJ 353 where Gopal Sri Ram JCA held that promotional items which were given away to customers who purchased the taxpayer's products were not entertainment expenses within section 39(1)(l) of the Act.

The High Court Judge then adopted the guidelines laid down by Gopal Sri Ram JCA (as His Lordship then was) in the *Aspac* case which are summarised as follows:

(1) The proper approach in determining whether expenses were incurred in the production of income is to examine the true nature of the transaction between the taxpayer and its customers.

(2) Where there is consideration moving from the customer to the taxpayer in the form of payment for the product sold, then the expenses incurred for (in this case) promotional items or gifts for the products are not entertainment expenses under the Act.

(3) Where the sole object of the activity undertaken was "*business promotion, the expenditure is not disqualified because the nature of the activity necessarily involves some other result, or the attainment or furtherance of some other objective, since the latter result or objective is necessarily inherent in the act*".

According to the High Court Judge, the '*business promotion*' aspect of the activity was the material consideration.

The High Court held that the incentive trips were not "entertainment" within the meaning of section 18 of the Act for the following reasons:

(1) the incentive trips were only given to those who achieved their sales target;

(2) achieving the sales target essentially meant that the sales of the company's product was being boosted and therefore income was increased;

(3) it did not matter that the incentive trips were also a reward to the dealers for their performance as the only reason it was given to them was because the sales target was achieved; and

(4) by virtue of the dealer's achievement of the sales target, there was consideration moving from the customer to KM in the form of payment for the product sold.

The High Court also went on to rule that the trips did not fall within the ambit of "hospitality" as mentioned in section 18 of the Act.

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GREAT EXPECTATIONS

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and was thus not reviewable by the Court. The Judge found this argument to be an afterthought as this policy was neither incorporated into the Circular nor were any questions regarding pregnancy raised during the interview for the post. The Circular furthermore did not specifically prohibit pregnant women from applying for the post, but merely stated that a teacher is not entitled to maternity leave.

The Defendants also argued that employing a pregnant woman to fill the GSTT post would defeat the purpose of the post which was to solve the problem of a shortage of teachers in Malaysia. Zaleha J rejected this argument and noted that the contract was on a monthly basis and could be terminated at any time. There was no guarantee that the GSTT would stay even if she was not pregnant. The court went on to further observe that the pregnancy would not necessarily interfere with the Plaintiff's duties as medical check-ups could be done outside school hours.

The learned Judge also rejected the Defendants' argument that it was justified in discriminating against pregnant women by virtue of the principle of reasonable classification. The Court noted that the concept was only applicable to Article 8(1) and not to Article 8(2) of the Federal Constitution. The Court relied on *PP v Datuk Harun Haji Idris & Ors* [1976] 1 LNS 180 where it was held that Article 8(2) contains particular application of the principle of equality and therefore discrimination solely on the grounds embodied under Article 8(2) cannot be justified by the use of the principle of reasonable classification.

The Defendants also submitted that Article 8 of the Federal Constitution does not apply to a contractual relationship. Applying *Beatrice AT Fernandez v Sistem Penerbangan Malaysia & Anor* [2005] 2 CLJ 713, the Court held that the Defendants are indisputably public authorities and thus agents of the Executive. Therefore, their actions fell within the ambit of Article 8(2) of the Federal Constitution.

The subsidiary issues raised in this case were, first, that the Plaintiff did not have locus to bring the action as there was no binding contract between the parties and, second, whether a declaration was a proper remedy. The learned Judge dealt with these points summarily by stating that the Plaintiff's right to be employed had been affected by the Defendants' decision and thus, the Plaintiff had locus to bring this action and as the Plaintiff was seeking to assert her right to a legal status, a declaration was the proper remedy to be sought.

COMMENTARY

The significance of this case is multifarious. Since time immemorial, Malaysia has been content with paying lip-service to its international human rights obligations, without giving pertinent international conventions legal recognition and the force of law. This decision marks a departure from the courts' complacent attitude towards international human rights law and is hopefully representative of an emergent rights-centred approach. The Court has finally realised the importance of interpreting domestic legislation in line with international law so as to ensure an improvement of Malaysia's reputation within the international human rights community.

In terms of women's rights, this decision is indeed long overdue. During the 35th session of CEDAW in 2006, the CEDAW committee expressed concern that CEDAW was not enforceable in Malaysian domestic courts and that no Malaysian legislation contained a proper definition of discrimination against women. Although it took more than half a decade, this case represents the first time our Malaysian courts have defined and discussed at length the concept of gender discrimination and used CEDAW to give effect to the provisions of the Federal Constitution.

Furthermore, while societal views of women in the workplace as a whole have evolved positively over the years, the law has been slow to reflect this. This decision will hopefully be an impetus for a positive trend of greater protection and promotion of woman's right in our courts. Both public and private sector employers would be forced to rethink their policies and guidelines to ensure compliance with the law.

It is also hoped that this case will give women the confidence to come to the forefront and report cases of discrimination to the authorities and to subsequently initiate legal action to seek redress for their grievances.

CONCLUSION

Leonardo da Vinci once said, *"I have been impressed with the urgency of doing. Knowing is not enough; we must apply. Being willing is not enough, we must do."* Malaysia has long known its place in the international community and the importance of international human rights and women's rights legislation. Finally, we have taken the bold step of giving it due recognition and legal status.

The Government has appealed against the decision. Whatever may be the outcome of the appeal, this ground-breaking decision will forever be remembered as one where our courts did what was plain and obviously just, without fear or favour.

As the Judge noted in the conclusion to her judgment, "*the court has a role to promote the observance of human rights in this country*". With this judgment as a guiding light, we can look forward to the courts' greater assumption of this role.

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A TALE OF TWO TAX CASES

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As "hospitality" was not defined in the Act, the Court referred to *United Detergent Industries Sdn Bhd v Director General of Inland Revenue* [1999] AMR 462 which defined "hospitality" as:-

"the action of entertaining someone without that person having to subscribe towards the cost incurred by the host for the purpose of entertaining that someone".

The Court held that KM was not being hospitable within the natural and ordinary meaning of the word as the trips were not given to all dealers but only to those who achieved their sales targets. In other words, only the dealers who contributed to and had generated more income for the company were awarded the trips.

"KM was not being hospitable within the natural and ordinary meaning of the word"

CONCLUSION

The effect of these decisions is that sales incentives paid or awarded by the taxpayer to its marketing agents or dealers who have achieved sales targets do not constitute entertainment expenses and are deductible expenses under section 33(1) of the Act.

While the Court of Appeal in the *NV Alliance Case* came to the same decision by looking only at the rules of statutory interpretation, the High Court in the *Khind Case* provided some helpful guidelines that a taxpayer can follow in the giving of sales incentives so as to ensure that the expenses are fully deductible against its gross income.

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COUNTING THE DAYS

The period of notice to be given by a company to its members for convening a general meeting is governed by its articles of association ("articles"). More often than not, the articles follow the requirements set out in the Companies Act 1965 ("CA").

For example, Section 145(1) of the CA provides that the period of notice for a general meeting convened for a purpose other than to pass a special resolution is to be not less than 14 days or such longer period as is provided in the articles.

The courts have on various occasions held that for the purpose of determining whether the minimum notice period specified in the articles have been complied with, the day on which the notice is issued and the day on which the meeting is to be held are to be excluded.

Bennet J in *Re Hector Whaling* [1936] Ch 208 held that the phrase "not less than twenty-one days" in Section 117(2) of the Companies Act 1929 means "*twenty-one clear days exclusive of the day of service and exclusive of the day on which the meeting is to be held.*"

The principle in *Re Hector Whaling* was followed in *Extreme System Sdn Bhd v Ho Hup Construction Company Bhd and Others* [2010] 1 LNS 338. In this case, the Malaysian High Court held that the minimum notice period of 28 days specified in Section 153 of the CA (for resolutions that require special notice) means 28 clear days, exclusive of the date of service of the notice and exclusive of the day on which the meeting is to be held.

The rules of interpretation adopted by the courts in the above-cited cases apply equally to the computation of the time periods specified in Sections 145(2A) and 152(1) of the CA which respectively prescribe a minimum notice period of 21 days for an annual general meeting of a public company and for a meeting convened to pass a special resolution.

It is important to ensure that the minimum time-frame prescribed by the articles of a company is complied with as the failure to do so may result in the proceedings at the meeting being invalidated.

LEGAL INSIGHTS

A SKRINE NEWSLETTER

SKRINE WAS FOUNDED ON 1ST MAY 1963 AND IS TODAY ONE OF THE LARGEST LAW FIRMS IN MALAYSIA. SKRINE IS A FULL-SERVICE FIRM DELIVERING LEGAL SOLUTIONS, BOTH LITIGATION AND NON-LITIGATION, TO NATIONAL AND MULTINATIONAL CLIENTS FROM A BROAD SPECTRUM OF INDUSTRIES.

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