



SURUHANJAYA SYARIKAT MALAYSIA
COMPANIES COMMISSION OF MALAYSIA

Review of the Companies Act 1965 - Final Report

by the
Corporate Law Reform
Committee (CLRC)





Review of the Companies Act 1965 - Final Report

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The image features a solid yellow background. A horizontal band of medium blue color spans the width of the image, positioned approximately in the middle. A thin, vertical white line runs from the top edge of the blue band down to the bottom edge of the image, located towards the right side. The word "Preface" is written in a white, serif font, centered horizontally within the blue band and positioned to the left of the vertical white line.

Preface

PREFACE

The Final Report (the Report) of the Corporate Law Reform Committee (CLRC) is the highlight of the Corporate Law Reform Programme that commenced in December of 2003. The Report comprises of the final recommendations and the reasons for such recommendations. This journey has been a long one, four years to be exact. The world of corporate law is complex and the CLRC in conducting the review of the Companies Act 1965 understood the need to ensure that the foundations of the corporate laws in Malaysia are designed in such a way that they will encourage sustainability and take into account the best interests of the companies, investors and society in the long run.

In conducting its review, the CLRC undertook various cross jurisdictional benchmarking studies of jurisdictions that have a similar corporate framework as Malaysia such as Australia, New Zealand, the UK, Hong Kong and Singapore. These jurisdictions possess similar legal frameworks as Malaysia and had undertaken their own respective review exercise of their corporate laws. The CLRC has studied their reviews thoroughly and has endeavoured to cull the best principles to suit the local corporate environment whilst always ensuring that they are up-to-date, competitive and designed to allow the local corporation to be 'global' in nature.

As Chairman of the CLRC, I would like to take this opportunity to express my heartfelt gratitude to the members of the CLRC and the various Working Groups who have unselfishly dedicated their time to this project. They have brought a wealth of knowledge and practical experience that allowed the CLRC to focus in the right direction and understand the practicality of the various legal requirements. I would also like to thank the Companies Commission of Malaysia (SSM) for giving the Committee the opportunity to spearhead this project and for the resources provided. To the industry players and the participants of the consultation process, I express, on behalf of the CLRC, our sincere appreciation for the various contributions and responses provided which have helped this project to amalgamate into a thorough and comprehensive review. Finally, I would

like to say a special thank you to Assoc. Prof. Dr Aiman Nariman Sulaiman and the Secretariat for their hard work, dedication and professionalism and the crucial role played in ensuring the success of this project.

Thank you,

Dato' K.C. Vohrah

Chairman

Corporate Law Reform Committee

Introduction

INTRODUCTION

The Corporate Law Reform Programme of the Companies Commission of Malaysia (SSM) began in December 2003 when the review of the Companies Act 1965 was initiated as part of SSM strategic direction in facilitating the development of a conducive and dynamic business and regulatory environment for this country.

SSM established the Corporate Law Reform Committee (CLRC) to spearhead the review of the Companies Act 1965 with the following objectives:

- to create a legal and regulatory structure that will facilitate business; and
- to promote accountability and protection of corporate directors and members taking into account the interest of other stakeholders, in line with international standards.

At the same time, when reviewing and recommending changes to the Companies Act 1965, the CLRC was to take into consideration the following factors:

- Modernising the law by taking into account the advances made in Information and Communication Technology (ICT);
- Reducing the costs of compliance;
- Reducing duplications and conflicts that exist between the various corporate regulatory bodies;
- Simplifying the existing operational processes of a company; and
- Simplifying the current legislative language as used in the Act.

As the backdrop of the reform exercise, these objectives guided the CLRC in its review of the core corporate law and corporate governance issues and practices that eventually became an integral part of this Report.

The Companies Act 1965 sets out the legal basis on which companies are formed, operated and managed. It also sets the rules on how directors and shareholders can exercise their rights as well as how their powers can be accounted for.

Since its enactment in 1965, the Companies Act 1965 has been updated through various piece-meal amendment exercises. All in all, there have been a total of 35 amendments to the Companies Act 1965, the most recent being the Companies (Amendment) Act 2007.

Some amendments were as a result of changes in the regulatory structure, whilst some were meant to address the weaknesses and inadequacies of the law and practices at the corresponding time. As these amendments were made on a piece-meal basis, they lacked a systematic and coherent review of current law and practices. Therefore, a review of the Companies Act 1965 is timely to better equip the business community to deal with future challenges in the face of an ever changing business environment.

The review allows modernisation and rationalisation of company law principles and practices by taking into account the development of trends in other jurisdictions particularly amongst the Commonwealth countries. Despite the fact that the Companies Act 1965 was modelled upon the Australian Uniform Companies Act 1961 many of its provisions are influenced by English company law principles and policies that are over 150 years old which may now no longer be in tandem with how businesses are managed and conducted presently.

Commonwealth countries, such as Australia, Canada, Singapore and New Zealand that once placed great reliance on the traditional English company law model have also chosen to abandon certain aspects of the English corporate law when reforming their respective corporate legislations. The United Kingdom had recently completed its review of the company law. These developments are strongly indicative of the need to modernise our corporate regulatory framework.

A sound corporate regulatory framework is necessary to promote enterprise, enhance competitiveness and stimulate investments. To this end, the CLRC strives to strike a balance between providing adequate rules for businesses to operate whilst at the same time providing necessary tools for the regulators to supervise the corporate community.

An effective and dynamic framework of company law and corporate governance is the key to a modern and robust economy.

The CLRC had, throughout the Law Reform Programme, issued a total of 12 consultative documents (CD) for public consultation. Such consultation process is a vital element to ensure that the views and feedback of the industry and stakeholders are taken into consideration when formulating the recommendations. This is especially important since the proposed recommendations will have a direct impact on the business community. Thus, the views and feedback play a significant part in ensuring that the proposed recommendations will facilitate and promote business growth. The 12 CDs are as listed below:

- (a) Strategic Framework for the Corporate Law Reform Programme of the Companies Commission of Malaysia (CD 1)
- (b) Capital Maintenance Rules and Share Capital: Simplifying and Streamlining Provisions Applicable to Shares (CD 2)
- (c) Engagement with Shareholders (CD 3)
- (d) Company Liquidation: Restatement of the Law (CD 4)
- (e) Clarifying and Reformulating the Directors' Role and Duties (CD 5)
- (f) Minority Shareholders' Rights and Remedies (CD 6)
- (g) Creating a Conducive Legal and Regulatory Framework for Businesses (CD 7)
- (h) Capital Maintenance Rules and Share Capital: Simplifying and Streamlining Provisions Applicable to the Reduction of Capital, Share Buy back and Financial Assistance Provisions (CD 8)

- (i) Review of Provisions Regulating Substantial Property Transactions (CD 9)
- (j) Reviewing the Corporate Insolvency Regime: The Proposal for the Corporate Rehabilitation Framework (CD 10)
- (k) Review of Criminal, Civil and Administrative Sanctions in the Companies Act 1965 (CD 11)
- (l) Auditors' Roles and Responsibilities (CD 12)

This Report contains a total of 188 recommendations that are reflective of modern business practices with the aim of simplifying laws and procedures to better facilitate business creativity and operations in Malaysia while ensuring accountability in corporate management and decision-making.

The recommendations of the Corporate Law Reform Committee (CLRC) are as follows:

Recommendation 1.1

The CLRC recommends that there should be a single statute that will apply to companies irrespective of whether the companies are small or large (in terms of ownership structure or economic size, etc).

Recommendation 1.2

The CLRC recommends that the distinction between public and private companies be retained and that this be used as a basis when simplifying and making company law more conducive to businesses.

Recommendation 1.3

The CLRC recommends that a private company should be defined as one where the Memorandum or Articles of Association:

- (a) provides that the number of its members shall not exceed 50;
- (b) restricts the right of its members to transfer their shares; and
- (c) prohibits an offer or issue of its shares (but not debentures) to the public.

Recommendation 1.4

The CLRC recommends the adoption of the definition of “an offer to the public” in relation to the restriction on public offers by private companies as stated in section 756 of the UK Companies Act 2006.

Recommendation 1.5

The CLRC recommends the retention of the requirements for all companies to keep accounting records and to prepare financial statements in accordance with the approved accounting standards.

Recommendation 1.6

The CLRC recommends the retention of mandatory audit rules for all companies but the regulator should be given power to exempt the application of the audit provision for certain types of companies based on certain criteria.

Recommendation 1.7

The CLRC recommends that the present rules in regard to filing of audited accounts be retained.

Recommendation 1.8

The CLRC recommends that the mandatory appointment of company secretaries for all types of companies be retained.

Recommendation 1.9

The CLRC recommends that there should be a register of company secretaries to be managed and controlled by SSM.

Recommendation 1.10

The CLRC recommends that newly formed companies should, unless the company otherwise elects, have the full capacity of a natural person and that existing companies be allowed to alter their Memorandum and Articles of Association to that effect.

Recommendation 1.11

The CLRC recommends that companies formed for any purpose referred to in section 24 of the Companies Act 1965 be still required to specify their objects.

Recommendation 1.12

The CLRC recommends that section 20 of the Companies Act 1965 be retained.

Recommendation 1.13

The CLRC recommends the abolishment of the doctrine of constructive notice except in so far it relates to the Register of Charges.

Recommendation 1.14

The CLRC recommends that the present classification of companies according to liability of members be retained.

Recommendation 1.15

The CLRC recommends that companies be allowed to incorporate with only a single member who can be the director who must be a natural person of full age and who has his principal place of residence within Malaysia.

Recommendation 1.16

The CLRC recommends that the mandatory name reservation process be done away with; and that the register of reserved names should be made available to the public.

Recommendation 1.17

The CLRC recommends that promoters have the option to reserve a name, for a shorter period.

Recommendation 1.18

The CLRC recommends that clear provision should be made in the Companies Act 1965 to exonerate the Registrar from liability under any civil action involving passing-off similar to section 11A(8).

Recommendation 1.19

The CLRC recommends that the Registrar should retain the power to direct name change.

Recommendation 1.20

The CLRC recommends that a single incorporation document in a prescribed form be introduced to simplify the incorporation process.

Recommendation 1.21

The CLRC recommends that the requirement for a statutory declaration be replaced with a requirement for a statement of compliance.

Recommendation 1.22

The CLRC recommends that the issuance of the certificate of incorporation be retained.

Recommendation 1.23

The CLRC recommends that the requirement for every company to have a common seal be retained.

Recommendation 1.24

To facilitate electronic filing and lodgement of documents, the CLRC recommends that:

- (a) the definition of “documents” under section 4(1) of the Companies Act 1965 be amended accordingly;
- (b) a person lodging a document electronically must keep a copy of the document and this must be made available to the Registrar, if so required; and
- (c) the present arrangement under section 11A(8) be retained, to protect the Registrar from liability against any loss or damage suffered by any person who obtains the documents which were electronically filed or lodged due to any error or omission of whatever nature and howsoever arising if the error or omission was made in good faith and in the ordinary course of the discharge of the Registrar's duties or if it occurred or arose as a result of any defect or breakdown in the service or equipment used for the provision of the service.

Recommendation 2.1

The CLRC recommends that the Companies Act 1965 should not require a private company to hold annual general meetings.

Recommendation 2.2

The CLRC recommends that in private companies member(s) holding at least 5% of the total voting shares may demand for an annual general meeting to be held.

Recommendation 2.3

The CLRC recommends that section 152A of the Companies Act 1965 be clarified to state that the written resolution procedure is not applicable in certain circumstances where special notice is required and that the written resolution procedures should be available to private companies only.

Recommendation 2.4

The CLRC recommends the removal of the unanimity rule for passing of written resolutions so that written resolutions may be passed by the same majority as required for a similar resolution at a duly convened meeting.

Recommendation 2.5

The CLRC recommends that companies be required to circulate the proposed written resolutions to all members who are entitled and eligible to vote.

Recommendation 2.6

The CLRC recommends that the requisite voting percentage for a written resolution must be obtained within a specified time frame of 28 days after the circulation of the proposed resolution and if the voting percentage is not obtained, the proposed resolution is deemed not carried.

Recommendation 2.7

The CLRC recommends that members holding at least 5 % of the total voting rights in a company should be given the right to request for a meeting to be convened.

Recommendation 2.8

The CLRC recommends that section 145A of the Companies Act 1965 be clarified to state that a primary venue for a meeting must be specified by the notice of the meeting and that the primary venue should still be in Malaysia.

Recommendation 2.9

The CLRC recommends that the Companies Act 1965 should facilitate the use of any technology that will allow shareholders reasonable opportunity to participate in meetings.

Recommendation 2.10

The CLRC recommends that the Companies Act 1965 should allow for other modes of communication (apart from the requirement that notices of meetings should be given personally or sent by post to shareholders) if shareholders agree.

Recommendation 2.11

The CLRC recommends the retention of the statutory provision allowing shareholders to circulate any proposed resolution and statement provided that the requisitionists meet the threshold requirements and the document for circulation consists of not more than 1,000 words.

Recommendation 2.12

The CLRC recommends amendment to section 151(4)(a)(i) of the Companies Act 1965 so that in the case of a requisition requiring notice of a resolution, a company should not be required to give notice of any resolution unless a copy of the requisition signed by the requisitionists is deposited at the registered office of the company not less than four weeks before the meeting.

Recommendation 2.13

The CLRC recommends that the company should be responsible for any costs in sending out the notice of the meeting to members if the company receives the notice in time (if it is deposited not less than four weeks before the meeting).

Recommendation 2.14

The CLRC recommends that section 149(1)(b) of the Companies Act 1965 be deleted.

Recommendation 2.15

The CLRC recommends against the introduction of any statutory provision requiring the disclosure of proxy voting information in the Companies Act 1965 but proposes that this issue be addressed by way of guidelines and best practices.

Recommendation 2.16

The CLRC recommends that the Companies Act 1965 be amended to enable direct absentee voting/ postal voting/ electronic voting. However, this should be facilitative rather than mandatory.

Recommendation 2.17

The CLRC recommends that voting by show of hands should not be prohibited by statute, but neither should it be made mandatory. Where proxy voting is concerned, proxies should be allowed to vote by show of hands but where a member appoints more than one proxy, the proxies should not be allowed to vote by a show of hands.

Recommendation 2.18

The CLRC recommends that the practice of bundling of proposed resolutions should not be regulated by statutory provisions but should be addressed by way of guidelines and best practices.

Recommendation 2.19

The CLRC recommends that there should not be any statutory formulation of the general functions and duties of the Chairman of a meeting. Instead, such roles and functions should be set out in non-legislative documents.

Recommendation 2.20

The CLRC recommends that section 144 of the Companies Act 1965 be clarified to enable a member or members holding not less than 5 % of the total voting rights to requisition a general meeting.

Recommendation 2.21

The CLRC recommends that section 145 of the Companies Act 1965 be amended to allow a member or members, holding not less than 5 % of the total voting rights to convene a meeting of the company.

Recommendation 2.22

The CLRC recommends that section 4 of the Companies Act 1965 should be amended by adding the words “the majority of the board of directors” to the present definition. The proposed amended definition would read as follows:

“any person occupying the position of a director of a corporation by whatever name called and includes a person in accordance with whose direction or instructions the majority of the board of directors of a corporation is accustomed to act and an alternate or substitute director”.

Recommendation 2.23

The CLRC recommends the deletion of section 124 and section 129 of the Companies Act 1965 and the amendment of section 122(2) of the Companies Act 1965 to clearly specify 18 as the minimum age for a person to be appointed as a director.

Recommendation 2.24

The CLRC recommends the retention of the residency requirement but in view of the recommendation for a “one member, one director” company, the CLRC recommends that the residency requirement should apply to at least one director of the company.

Recommendation 2.25

The CLRC recommends the retention of section 126 of the Companies Act 1965 that requires the resolution to appoint a director of a public company to be voted on individually.

Recommendation 2.26

The CLRC recommends that the right of the shareholders at a general meeting to remove a director (as reflected in section 128 of the Companies Act 1965) should be made applicable to public companies only and should not be extended to private companies.

Recommendation 2.27

The CLRC recommends that section 128(2) of the Companies Act 1965 be amended to state that where a director of a public company is to be removed, special notice is required only when the director is to be removed in accordance with section 128 of the Companies Act 1965.

Recommendation 2.28

The CLRC recommends that a resigning director should have the right to lodge his notice of resignation to the Registrar at any time after notice of his resignation has been communicated to the company. This right however is subject to the requirement that there should be at least one director of a company at any one time.

Recommendation 2.29

The CLRC recommends the introduction of a statutory provision that requires the remuneration of directors of public companies to be approved specifically by shareholders at general meeting. Shareholders and members of a company should be given inspection rights of the directors' contracts of service if requested by (a) members with not less than 5 % shareholding or (b) at least 100 members who are entitled to vote at a general meeting.

Recommendation 2.30

The CLRC recommends the retention of section 137 of the Companies Act 1965 with the amendment that the compensation for loss of office for a public company shall be approved by disinterested shareholders.

Recommendation 2.31

The CLRC recommends that where a subsidiary is going to make a payment to its director (whether or not that director is also a director of its holding company) pursuant to section 137 of the Companies Act 1965, that payment should be approved by the shareholders of the holding company in addition to the shareholders of the subsidiary company.

Recommendation 2.32

The CLRC recommends against the codification of obligations of corporate social responsibility (i.e., the relationship between a company and its creditors and employees) under the Companies Act 1965.

Recommendation 2.33

The CLRC recommends the retention of section 140(1) of the Companies Act 1965.

Recommendation 2.34

The CLRC recommends that a company be allowed to provide indemnity for any costs incurred by a director, officer or auditor in defending legal proceedings, whether civil or criminal, only when the director, officer or auditor is successful (whether by a judgment in his favour, an acquittal or by a discontinuance).

Recommendation 2.35

The CLRC recommends that a company should not be allowed to purchase or maintain insurance for directors, officers or auditors in relation to liability owed towards the company.

Recommendation 2.36

The CLRC recommends that section 140 of the Companies Act 1965 should be clarified to allow a company to purchase or maintain insurance or to indemnify its officer or director or auditor for cost, expenses and liability incurred by that officer or director or auditor in defending an action commenced by a third party (the third party being a person other than the company).

Recommendation 2.37

The CLRC recommends that any insurance or indemnification that is allowed to be taken by the company for its directors or officers or auditors (as stated in recommendation 2.36) will have to be disclosed to shareholders.

Recommendation 2.38

The CLRC recommends that section 181 of the Companies Act 1965 should be clarified to state that the remedy thereunder is available where the effect of the conduct complained about persists at the time the application is made.

Recommendation 2.39

The CLRC recommends that section 181 of the Companies Act 1965 should be amended to give standing to, in addition to the existing persons who can bring an action under the oppression provision (i.e., members and debenture holders), the following persons:

- (a) a person who is a former member but only if the oppression relates to the circumstances in which he ceased to be a member.
- (b) a transferee of shares or a person entitled to them by operation of law whose membership has not yet been perfected (i.e., beneficial owner).

Recommendation 2.40

The CLRC recommends that the statutory derivative action should be made applicable to all types of companies.

Recommendation 2.41

The CLRC recommends that the common law derivative action should be replaced by the statutory derivative action.

Recommendation 2.42

The CLRC recommends that the statutory derivative action may be brought by any member or director of the company or any person who at the discretion of the court, is a proper person to make an application under this section.

Recommendation 2.43

The CLRC recommends that a variation of class rights can be done:

- if written consent is obtained from at least 75% of the shareholders whose rights are to be varied; or
- if a special resolution is passed at a separate class meeting of shareholders whose rights are to be varied.

Recommendation 2.44

The CLRC recommends the class rights should be capable of being entrenched in the Memorandum. However, entrenchment should not be absolute in that those rights can still be varied but only with the unanimous consent of that class of shareholders whose rights are to be varied.

Recommendation 2.45

The CLRC recommends that the present law that the statutory procedure applies only where the company has issued more than one type of shares be retained.

Recommendation 2.46

The CLRC recommends that section 65(6) and (7) of the Companies Act 1965 be retained.

Recommendation 2.47

The CLRC recommends that where a company proposes to redeem or cancel preference shares (except in the case of redeemable preference shares), this should be statutorily provided as a variation of the rights of the existing preference shareholders.

Recommendation 2.48

The CLRC recommends against the codification of a compulsory minority buy out provision and against the codification of a class action remedy in the Companies Act 1965.

Recommendation 2.49

The CLRC recommends that the existing requirement as to the appointment of an auditor for both public and private companies should be retained.

Recommendation 2.50

The CLRC recommends that in relation to the duration of appointment of auditors for private companies, the duration be in accordance with the terms of appointment, until the auditor is removed by shareholders at a general meeting or until the auditor resigns.

Recommendation 2.51

The CLRC recommends that the current statutory provisions under section 172(1) and (2) of the Companies Act 1965 relating to the appointment of auditors be retained.

Recommendation 2.52

The CLRC recommends that section 172(14) and (15) of the Companies Act 1965 be amended to the following effect. In the case of the resignation of auditors, the effective date of resignation would be at the end of 21 days from the time the notice is deposited with the company. The directors must proceed duly within the 21 days to convene a meeting on a day not more than 28 days after the date on which the notice convening the meeting is given. Every director who fails to take all reasonable steps to secure that a meeting is convened as mentioned above shall be guilty of an offence and liable to a fine.

Recommendation 2.53

The CLRC recommends that in the case of the resignation of an auditor of a public listed company, the auditor should be required to submit a resignation statement stating either that there are no circumstances connected with his resignation that need to be brought to the attention of members or creditors of the company, or to set out the circumstances for his resignation. The resignation statement should be submitted to the company and the company should be required to circulate it to shareholders. This duty should be in addition to the duty to inform the regulators upon ceasing to hold office as auditor under section 172A of the Companies Act 1965.

Recommendation 2.54

The CLRC recommends against a codification of the mandatory rotation of audit firms and recommends that rules relating to mandatory audit rotation should continue to be a matter of best practice.

Recommendation 2.55

The CLRC recommends the enactment of a statutory provision giving the auditor the right to be provided all communications relating to any resolutions which the company proposes to pass by way of the written resolution procedure.

Recommendation 2.56

The CLRC recommends against codification of the categories of persons to whom auditors owe a duty of care and recommends that any development should be left to case laws on a case to case basis.

Recommendation 2.57

The CLRC recommends the retention of the current regime that relies on statute to state the general duty of auditors to report whether the accounts give a true and fair view of the company's financial position while relying on best practice and self-regulation to provide guidance on whether the accounts give a true and fair view of the company's financial position.

Recommendation 2.58

The CLRC recommends that an independent Auditing Oversight Body should be established comprising persons other than members from the professional accounting bodies such as regulators, investor associations and industry associations. This proposed body should be responsible for the inspection of auditors to ensure that they comply with international and domestic auditing and ethical standards as well as be responsible for the investigation and the imposition of proportionate sanctions on errant auditors. This proposed body will co-exist with professional accounting bodies which would be responsible for the professional functions of the audit profession.

Recommendation 2.59

The CLRC recommends that the requirement for disinterested shareholders' voting to approve substantial property transactions under sections 132C and 132E of the Companies Act 1965 should only be applicable to public companies.

Recommendation 2.60

The CLRC recommends that the threshold of substantial value under sections 132C and 132E of the Companies Act 1965 in respect of a transaction in relation to non-public listed companies should be as follows-

- (a) if the transaction exceeds 10 % of the company's net assets value and is more than RM50,000; or
 - (b) if the transaction exceeds RM250,000,
- and that the net assets are to be determined by reference to the most recent financial statements.

Recommendation 2.61

The CLRC recommends that a transaction entered into in contravention of section 132C and 132E of the Companies Act 1965 be voidable by the company. The CLRC also recommends that, bona fide third parties must be protected and that a transaction or arrangement entered into without shareholders' approval cannot be avoided by a company in the following instances:

- (a) where restitution of any money or other asset that was the subject matter of the transaction is no longer possible;
- (b) where the company has been indemnified for any loss or damage resulting from the transaction; or
- (c) where rights are acquired in good faith, for value and without actual notice of the contravention by a person who is not a party to the transaction.

Recommendation 2.62

The CLRC recommends to amend section 122A(2) of the Companies Act 1965, i.e. the definition of “persons connected to directors” to state:

“In paragraph (1)(a) the members of the director's family are his spouse, parent, child (including adopted child and step child), brother, sister and the spouse of his child, brother or sister.”

Recommendation 2.63

The CLRC recommends the definition of “a body corporate associated with a director” be as follows:

“For the purposes of paragraph (1)(b) a body corporate is associated with a director if-

- (a) the body corporate is accustomed or is under an obligation, whether formal or informal, or its majority of directors are accustomed, to act in accordance with the directions, instructions or wishes of that director; or
- (b) that director has a controlling interest in the body corporate; or
- (c) that director or a person connected with him, or that director or persons connected with him, are entitled to exercise, or control the exercise of, not less than 20% of the votes attached to voting shares in the body corporate.”

Recommendation 2.64

The CLRC recommends that the meaning of “controlling interest” or the concept of control be defined under section 122A(3)(b) be as follows:

“A person is deemed to have control or have a controlling interest in a body corporate if the person or persons connected to him or the person together with persons connected to him-

- (a) holds more than 50% of the issued share capital of the body corporate; or
- (b) controls more than 50% of the voting power of the body corporate; or
- (c) is able to control the composition of the board of directors of the body corporate.”

Recommendation 2.65

The CLRC recommends that section 6(4) of the Companies Act 1965 be amended to state:

"A person shall be deemed to have an interest in a share where a body corporate has an interest in that share and-

- (a) the body corporate, or a majority of its directors are accustomed, or is under an obligation, whether formal or informal, to act in accordance with the direction, instructions or wishes of that person in relation to that share;
- (b) that person has a controlling interests in the body corporate; or
- (c) that person or the associates of that person or that person and his associates are entitled to exercise or control the exercise of not less than 20% of the votes attached to the voting shares in the body corporate."

Recommendation 2.66

The CLRC recommends no changes to the ambit and scope of sections 133 and 133A of the Companies Act 1965. The CLRC also recommends not to extend sections 133 and 133A to "substantial shareholders" or "person connected to shareholders".

Recommendation 2.67

The CLRC recommends to retain section 131 to the effect that that a director must disclose his direct or indirect interest in any contract or proposed contract with the company to the board of directors of his company where there exists a conflict or potential conflict of interest in respect of that contract or proposed contract, be retained.

Recommendation 2.68

The CLRC recommends that a director should only be made accountable for contravening section 131 if he is aware of the interest and intentionally does not disclose the interest.

Recommendation 2.69

The CLRC recommends that any declaration under of interest under section 131 of the Companies Act 1965 must be made in accordance with any of the following methods:

- (a) at a meeting of the board of directors
- (b) by notice in writing
- (c) by giving a general notice of future conflict of interest pursuant to section 131(4) of the Companies Act 1965.

Recommendation 2.70

The CLRC recommends:

- (a) to retain the current threshold of 5% as is currently provided for by section 69D;
- (b) to retain the current timeline of seven days for giving the required notice to the company pursuant to sections 68E, 69F and 69G of the Companies Act 1965.

Recommendation 2.71

The CLRC recommends that there is no necessity to propose a threshold or de minimis rule for section 69F of the Companies Act 1965.

Recommendation 3.1

The CLRC recommends that:

- (a) companies limited by shares be no longer required to state its authorised share capital in the company's Memorandum;
- (b) all shares of a company should no longer have a par value attached to them; and
- (c) the conversion of all shares to shares of no par value should be made mandatory for all companies as at and from the date to be specified as the conversion date.

Recommendation 3.2

The CLRC recommends that companies under the no par value (NPV) regime should be authorised to elect to capitalise their profits without having to increase the number of shares owned by a shareholder (i.e. without any issue of new shares to shareholders), to capitalise their profits coupled with the issue of new shares to shareholders or to consolidate and subdivide the NPV shares.

Recommendation 3.3

The CLRC recommends that companies shall be permitted after the conversion date to issue redeemable preference shares (RPS) without having to maintain a capital redemption reserve when the RPS are redeemed. If the redemption of the RPS is made out of available profits, the company is required to transfer the amount redeemed to the company's contributed capital account.

Recommendation 3.4

The CLRC recommends that the amount standing to the credit of the share premium account and the capital redemption reserve should be capable of being utilised during the transitional period for:

- (a) providing premium payable on the redemption of RPS issued before that date;
- (b) writing off preliminary expenses of the company incurred before that date; and
- (c) writing off expenses incurred, or commissions or brokerages paid or discounts allowed, on or before that date, for any duty, fee or tax payable on or in connection with any issue of the company's shares.

Recommendation 3.5

The CLRC recommends that the shareholder's liability for any unpaid portion of the issue price of shares should not cease after the conversion date.

Recommendation 3.6

The CLRC recommends that sections 58, 56(1) and 57 of the Companies Act 1965 should be retained and section 56(2) of the Companies Act 1965 should be abolished.

Recommendation 3.7

The CLRC recommends that a time frame of two years be given as a transitional period for all companies to utilise the amount standing to the credit of their share premium account, if any.

Recommendation 3.8

The CLRC recommends the retention of section 64 of the Companies Act 1965. The CLRC also recommends the introduction of an alternative procedure for reduction of capital where a solvency test requirement will have to be fulfilled by the company when initiating a reduction of capital exercise. In such a situation, the confirmation of the court should not be required.

Recommendation 3.9

The CLRC recommends the introduction of a statutory solvency test, as follows:

“The company is able to satisfy the solvency test if-

- (a) the company is able to pay its debts as they become due in the normal course of business (cash-flow solvency); and
- (b) the value of the company's assets is greater than the value of its liabilities, including contingent liabilities (balance sheet solvency).

In determining whether the value of the company's assets is not less than the value of its liabilities, the directors:

- (a) must have regard to -
 - (i) the most recent financial statement of the company; and
 - (ii) all other circumstances that, the directors know or ought to know, affect or may affect the value of the company's assets and the value of the company's liabilities, including its contingent liabilities.
- (b) may rely on valuations of assets or estimates of liabilities that are reasonable in the circumstances."

The solvency statement which must be made by the directors must state :

- (a) that they have formed the opinion that, as regards the company's situation at the date of the statement, there is no ground on which the company could then be found to be unable to pay its debts; and
- (b) that they have formed the opinion -
 - (i) if it is intended to commence winding up of the company within the period of 12 months immediately following the date of the statement, that the company will be able to pay its debts in full within the period of 12 months beginning with the commencement of the winding up; or
 - (ii) if it is not intended so to commence winding up, that the company will be able to pay its debts as they fall due during the period of 12 months immediately following the date of the statement.

Recommendation 3.10

The CLRC recommends the introduction of a provision to hold any director criminally liable for any false declaration made regarding the solvency status of the company.

Recommendation 3.11

The CLRC recommends that a provision on arriving at the list of creditors be included as part of the capital reduction provisions.

Recommendation 3.12

The CLRC recommends that creditors be enabled to object to the reduction of capital exercise by the company (whether private or public). The objection may be made within four weeks after the special resolution is passed. The grounds for objection should be specified in the statutory provision and that these are where the creditors have not been offered security for the debts or any other safeguards or that the company does not have sufficient assets.

Recommendation 3.13

The CLRC recommends that where a creditor objects to a capital reduction exercise but does not have reasonable grounds to object, he should be liable for costs incurred.

Recommendation 3.14

The CLRC recommends that in the event that a company becomes unable to pay its debts within the period specified in the solvency statement, such company should be entitled to recover from its members the amount which they have received as a result of the reduction of capital of the company except where the distribution was received in good faith.

Recommendation 3.15

The CLRC recommends the introduction of a solvency test for a share buy back. The declaration of solvency is to be made by a majority of the directors.

Recommendation 3.16

The CLRC recommends the removal of the words “on the market of the Stock Exchange on which the shares are quoted” in section 67A(3B)(b) of the Companies Act 1965. This will enable treasury shares to be sold not just on the stock exchange but also via direct business transactions.

Recommendation 3.17

The CLRC recommends that section 67A(3C) of the Companies Act 1965 should clearly state that a company shall have no voting rights or the right to share in any distribution (i.e., dividends or distribution of assets upon a winding up) attached to its treasury shares and that the treasury shares are to be treated as carrying no voting rights but shall continue to be ordinary shares of the company.

Recommendation 3.18

The CLRC recommends that:

- (a) a company be permitted to give financial assistance for the purpose of or in connection with the purchase of or subscription for its shares or shares in its holding company provided the company is able to satisfy the solvency test and provided that a special resolution is passed by its shareholders to authorise the giving of such financial assistance;
- (b) the solvency test proposed for a reduction of capital and share buy back be adopted for such financial assistance;
- (c) the solvency statement be made by a majority of the directors and personal liability be imposed on the directors for making a statement which is not based on reasonable grounds.

Recommendation 4.1

The CLRC recommends that section 219(2) of the Companies Act 1965 be amended to provide that the commencement date of a compulsory winding up is the date the order to wind up the company is made by the court.

Recommendation 4.2

The CLRC recommends the introduction of a list of exempt dispositions so that transactions which are exempt dispositions do not require any validation order from the court.

Recommendation 4.3

The CLRC recommends removing any cross-referencing to the provisions of the Bankruptcy Act 1967 on issues relating to undue preference transactions under section 293 of the Companies Act 1965 and that, all provisions concerning undue preference transactions under the Bankruptcy Act 1967 and any other statutes be incorporated into the Companies Act 1965.

Recommendation 4.4

The CLRC recommends the introduction of a list of undue preference transactions by incorporating within the Companies Act 1965 all provisions on undue preference transactions in respect of companies winding up currently under the purview of section 53 of Bankruptcy Act 1967.

Recommendation 4.5

The CLRC recommends that section 295 of the Companies Act 1965 should be extended to 'connected persons' which has reference to section 122A of the Companies Act 1965. In relation to a compulsory winding up, the claw back period should be six months from the date of the presentation of a petition for winding up by the court. For clarity only the words "commencement of winding up" would be replaced with "the date of presentation of petition for winding up to the court".

Recommendation 4.6

The CLRC recommends that the threshold of statutory debts under section 218(2) of the Companies Act 1965 be increased to RM5,000.

Recommendation 4.7

The CLRC recommends that the time frame within which a petition for winding up must be filed should be six months from the expiry of the notice of demand. However, no leave of court should be required to issue a statutory demand afresh.

Recommendation 4.8

The CLRC recommends:

- (a) that the court be given the power to terminate winding up proceedings on the application of a relevant party; and
- (b) that an application to terminate winding up proceedings may be made by a liquidator, or a director or shareholder of the company or any other entitled person or a creditor of the company, or the Registrar.

Recommendation 4.9

The CLRC recommends that section 231 of the Companies Act 1965 be clarified by stating that "the court may appoint the Official Receiver or an approved liquidator as interim liquidator at any time after the presentation of a winding up petition and before the making of a winding up order...".

Recommendation 4.10

The CLRC recommends as follows:

- (a) that the prior approval of the court or the Committee Of Inspection be not required before an advocate could be appointed.

- (b) that a liquidator be empowered to compromise debts owed to the company if the amount is less than RM10,000 and this power should be exercisable without the having to obtain the sanction of the court.
- (c) that the court or the Committee Of Inspection be given a discretionary power to give a blanket approval to liquidators to compromise debts which are above the threshold of RM10,000 but not more than RM50,000 and this power should be exercised on a case to a case basis.
- (d) that the existing time frame for a liquidator to trade after the winding up order has been made be extended to six months, after which the liquidator be required to obtain the sanction of the court.
- (e) that section 238(2) of the Companies Act 1965 be deleted.
- (f) that section 234 of the Companies Act 1965 be amended by deleting the requirement for company secretaries to submit statements of affairs.
- (g) that the current mandatory requirement to settle a list of contributories be amended to make it discretionary for the liquidator to settle the list of contributories if there should be surplus capital for distribution or if there should be contributories who are likely to contribute their unpaid portion of capital.

Recommendation 4.11

The CLRC recommends the codification of the rights of secured creditors in the Companies Act 1965 along the lines of section 305 of the New Zealand Companies Act 1993.

Recommendation 4.12

The CLRC recommends that the provisions in relation to proof of debts be retained and that all the provisions relating to the proof of debts and the rank of claims by creditors as currently stated in the Bankruptcy Act 1967 be incorporated into the Companies Act 1965.

Recommendation 4.13

The CLRC recommends that the right of set-off should not be applicable to creditors "if the creditor has notice at the time the sums owed became due that a meeting of creditors has been summoned or a petition for the winding up of the company was pending".

Recommendation 4.14

The CLRC recommends retaining section 292 of the Companies Act 1965.

Recommendation 4.15

The CLRC recommends increasing the quantum for wages and salary of employees entitled to priority in the winding up of a company from the present RM1,500 to RM15,000.

Recommendation 4.16

The CLRC recommends excluding "payment of gratuity for termination of employment" from the definition of "wages and salary of employees" in section 292 of the Companies Act 1965.

Recommendation 4.17

The CLRC recommends abolishing any preference given in the winding up of a company to the government in respect of any unpaid taxes of a company under liquidation.

Recommendation 4.18

The CLRC recommends that the court should be empowered to make a judicial management order in relation to a company if it is satisfied that the company is or will be unable to pay its debts and it considers that the making of the order would be likely to:

- (a) achieve the company's survival on the whole or in part; and
 - (b) enable a more advantageous realisation of the company's assets than in a winding up.
- For this purpose, a company "will be unable to pay its debts" if any of the circumstances as stated in section 218(2) of the Companies Act 1965 should arise.

Recommendation 4.19

The CLRC recommends that parties who may be entitled to apply for a judicial management order be the company or its directors (pursuant to an ordinary resolution of its members or a resolution of the board of directors) or a creditor or creditors of the company (including prospective and contingent creditors). However, the court should not make the order if:

- (a) a receiver and manager has been or will be appointed or the making of the order is opposed by a person who is entitled to appoint a receiver and manager, e.g. a debenture holder; or
- (b) the company is in liquidation or the company is a bank or a finance company or an insurance company licensed under the relevant Act.

Recommendation 4.20

The CLRC recommends that when an application for a judicial management order is made to the court, the notice of the application should be served on:

- (a) the company with respect to which the order is sought to be made, in a case where a creditor is the applicant; and
- (b) to any person who has appointed or is or may be entitled to appoint a receiver and manager of the whole (or substantially the whole) of such company's property under the terms of any debenture of such company.

Recommendation 4.21

The CLRC recommends that once a petition for a judicial management order has been made, an interim judicial manager may be appointed by the court, although this should not be required in all situations. The CLRC further recommends that during the period beginning with the making of an application for a judicial management order and ending with the making of such an order or the dismissal of the application:

- (a) no resolution should be passed or order made for the winding up of the company;

- (b) no steps should be taken to enforce any charge or security over the company's assets without leave of the court; and
- (c) no proceedings against the company should be commenced or continued without leave of the court.

Recommendation 4.22

The CLRC recommends that at the hearing of an application for a judicial management order, the court should be entitled to exercise its discretion in deciding whether or not to make a judicial management order. Once a judicial management order is made, a moratorium should be in place during which:

- (a) no winding up order can be made against the company and any petition for winding up shall be dismissed;
- (b) any receiver and manager appointed shall vacate office and no new appointment of any receiver and manager shall be permitted;
- (c) no enforcement of any charge or security or repossession of hire purchase goods shall be permitted;
- (d) no other legal proceedings against the company shall be commenced or continued except with leave of the court.

Recommendation 4.23

The CLRC recommends that with the exception of companies listed on the Bursa Malaysia Securities Berhad any transfer of shares or any alteration in the status of members of a company with respect to which a judicial management order has been made during the moratorium period shall be void unless the court otherwise orders.

Recommendation 4.24

The CLRC recommends that the judicial manager should be given 180 days to table a proposal to creditors, and where appropriate the court should be entitled to give an extension of time to the judicial manager to do so but the maximum duration of the moratorium should be one year after the order appointing the judicial manager is made.

Recommendation 4.25

The CLRC recommends that the moratorium which takes effect upon the appointment of a judicial manager should be effective for 180 days from the date the order is made unless earlier discharged or further extended by the court.

Recommendation 4.26

The CLRC recommends that:

- (a) utility suppliers with monopolistic control such as Tenaga Nasional Berhad (TNB), Telekom, etc should be obliged to continue to provide supplies to a company with respect to which a judicial management order has been made so long as new debts incurred by such company are paid;
- (b) no steps be permitted to be taken to commence or to continue the enforcement of a sale of land of such a company under the National Land Code except with the leave of the court.

Recommendation 4.27

The CLRC recommends that a statutory provision be enacted stating that the limitation period shall not run with respect to any cause of action against a company in relation to which a judicial management order has been made during the moratorium period and that the moratorium period should be excluded for the purpose of calculating the limitation period.

Recommendation 4.28

The CLRC recommends that at a creditors meeting convened to consider a proposal tabled by the judicial manager, not less than a 75% majority in value of creditors, present and voting either in person or by proxy, whose claims have been accepted by the judicial manager, be the requisite majority to approve the proposal with modifications, subject to the judicial manager's consent to each modification.

Recommendation 4.29

The CLRC recommends that any secured creditor be given the right to oppose the petition or application for a judicial management order. However, once the judicial management order has been made the secured creditors should not be permitted to realise their security and the judicial manager should have the power to deal with the charged property of the company as if the property were not subject to the security. There should also be an express statutory provision that once the proposal is approved, it shall be binding on all creditors of the company whether or not they have voted in favour of the proposal.

Recommendation 4.30

The CLRC recommends that the judicial manager should be required to report the result of the creditors' meeting to the court and to notify the Registrar of the same. In addition, the decision of the creditors' meeting should be advertised in the national daily newspapers, at least one in English and one in Bahasa Malaysia.

Recommendation 4.31

The CLRC recommends that creditors should be able to bring an action for relief against oppressive conduct if the court is satisfied that company's affairs, property or business are being or have been managed by the judicial manager in a manner which is or was unfairly prejudicial to the interests of its creditors or members generally or of some part of its creditors or members.

Recommendation 4.32

The CLRC recommends that the judicial management order should be discharged in the following situations:

- (a) if the proposal has not been approved by the requisite majority in the creditors' meeting and where the court orders the discharge of the judicial manager. The court should be entitled by order to discharge the judicial management order and make such consequential provision as it thinks fit, or adjourn the hearing conditionally or unconditionally, or make an interim order or any other order that it thinks fit;
- (b) if the purpose of the judicial management has been successfully achieved;
- (c) if the judicial manager is of the view that the purpose of judicial management is unachievable;
- (d) if the judicial manager applies for a discharge, or is no longer qualified to be a judicial manager or is removed from office, unless the court makes an order replacing the existing judicial manager.

Recommendation 4.33

The CLRC recommends that the powers of the judicial manager should be expressly provided for in the companies legislation and the adoption of the powers of the judicial manager as stipulated under section 227G of the Singapore Companies Act (Chapter 50).

Recommendation 4.34

The CLRC recommends that the judicial manager should be deemed to be the agent of the company during the period of judicial management.

Recommendation 4.35

The CLRC recommends that the judicial manager should be given control over the affairs, business and property of the company during the judicial management period.

Recommendation 4.36

The CLRC recommends the suspension of powers of the other officers of the company during the judicial management period unless written approval is obtained from the judicial manager.

Recommendation 4.37

The CLRC recommends that a company secretary should not be exempted from the duty to submit the statement of affairs to the judicial manager.

Recommendation 4.38

The CLRC recommends that a judicial manager should be allowed to exclude personal liability in any contract entered into by him or adopted by him so that he is personally liable unless he disclaims such liability.

Recommendation 4.39

The CLRC recommends that a judicial manager should be indemnified in respect of his liabilities, remuneration and expenses, out of the assets of the company in priority to all other debts except those subject to security of a non-floating nature.

Recommendation 4.40

The CLRC recommends the introduction of a statutory Corporate Voluntary Arrangement scheme along the lines of that provided under the laws of the UK, with modifications, if necessary.

Recommendation 4.41

The CLRC recommends that the moratorium period should apply to both small and large companies seeking to propose a Corporate Voluntary Arrangement scheme in its rehabilitation process.

Recommendation 4.42

The CLRC recommends that a moratorium period for a Corporate Voluntary Arrangement scheme should be automatically in force upon the filing of relevant documents in court without the need for a court order.

Recommendation 4.43

The CLRC recommends that a moratorium period for a Corporate Voluntary Arrangement scheme may be extended for up to 60 days if both the creditors and the insolvency practitioner agree to it.

Recommendation 4.44

The CLRC recommends that the court's involvement in a Corporate Voluntary Arrangement scheme should be limited to hearing challenges to such scheme on the grounds of material irregularity, or unfair prejudice to the interest of a creditor or member or that the scheme is anticipated to be ineffective in practice.

Recommendation 4.45

The CLRC recommends that the proposal for a Corporate Voluntary Arrangement scheme may be approved by a majority vote of not less than 75% of the total value of the creditors who may vote in person or by proxy and that the proposal as so approved would be binding on the creditors of the company and that any modifications to the proposal should not be allowed. If there were any modifications, the creditors should vote on any modified proposal in the next meeting. The result of the meeting should also be reported to the court.

Recommendation 4.46

The CLRC recommends that a Corporate Voluntary Arrangement scheme itself or the procedure involved in its approval should be subject to challenge in court. An application for such challenge should be made within 28 days beginning with the first day the report is made to the court. If a creditor alleges that he has not been given notice, he should be entitled to challenge the decision of the meeting within 28 days of the day on which he became aware that the meeting had taken place.

Recommendation 4.47

The CLRC recommends that the management of a financially distressed company under a Corporate Voluntary Arrangement scheme should remain with the directors.

Recommendation 4.48

The CLRC recommends that if the 90-day period of the moratorium for a scheme of arrangement between a company and its creditors is extended, it should be limited to not more than one year.

Recommendation 4.49

The CLRC recommends the appointment of a qualified insolvency practitioner to assess the viability of a scheme of arrangement between a company and its creditors.

Recommendation 4.50

The CLRC recommends that the moratorium for a scheme of arrangement between a company and its creditors should not be effective against the companies and securities market regulators so as to prevent them from commencing any enforcement actions to ensure compliance of corporate and/or securities law or guidelines thereunder.

Recommendation 4.51

The CLRC recommends that:

- (a) the agency status of the receiver or a receiver and manager be codified.
- (b) once a company is in liquidation and a liquidator has been appointed, a receiver should be empowered to continue to act as the agent of the company, to carry on the business of the company provided he obtains consent from the liquidator which must not be unreasonably withheld, or if the liquidator withholds his consent, the consent of the court;
- (c) the agency status of the receiver or receiver and manager over the assets secured under the debenture should continue after the appointment of the liquidator.

Recommendation 4.52

The CLRC recommends that there should be a codification of a minimum list of powers which should be applicable as a default provision in case the debenture is silent as to the powers of a receiver.

Recommendation 4.53

The CLRC recommends that a receiver should be personally liable for debts incurred by him or his authorised agents during his tenure of office, unless there is a specific agreement to the contrary between the contracting parties.

Recommendation 4.54

The CLRC recommends that a receiver should have the right to be indemnified out of the assets of the company which are charged under the debenture pursuant to which the receiver is appointed.

Recommendation 4.55

The CLRC recommends that the receiver's cost and remuneration should be given priority over all claims by other creditors.

Recommendation 4.56

The CLRC recommends that:

- (a) the requirement that a charge which is required to be registered under the Companies Act 1965 be registered within 30 days of the date of its creation be retained, and
- (b) a charge be given priority from the date of its creation once it has been registered with the Registrar.

Recommendation 4.57

The CLRC recommends deletion of section 108(9) of the Companies Act 1965.

Recommendation 4.58

The CLRC recommends retaining the provision on dual registration of charges.

Recommendation 4.59

The CLRC recommends modifying Form 34 to include the words “the interested party”.

Recommendation 4.60

The CLRC recommends the retention of the current system for the registration of charges but acknowledges that, having a list of registrable and non-registrable charges is another option and the risk of the list being construed as exhaustive can be mitigate against with proper drafting of the section.

Recommendation 5.1

The CLRC recommends that the regulator should be authorised to bring either criminal or civil proceedings for any contravention of the statutory provisions on directors' duties.

Recommendation 5.2

The CLRC recommends that criminal liability for the contravention of directors' duties should be imposed where the contravention is accompanied by fraud or dishonesty. Where there is no such fraud or dishonesty, the contravention should not be criminalised but the regulator should be empowered to bring civil proceedings.

Recommendation 5.3

The CLRC recommends that there should be criminal liability imposed for non-compliance with disclosure obligations. Where the non-compliance relates to other procedural requirements, such failures to comply should not give rise to criminal liability.

Recommendation 5.4

The CLRC recommends that in cases where a contravention involves fraud or deliberate wrongdoing or dishonesty, criminal liability should be imposed on officers involved in the contravention and not the company.

Recommendation 5.5

The CLRC recommends that the general penalty provision under section 369 of the Companies Act 1965 should be revised to reflect the view that whether or not there should be criminal liability for a contravention of any section of the Companies Act 1965 should be decided on a "section by section" basis.

Recommendation 5.6

The CLRC recommends that in the case of non-compliance with procedural requirements, criminal liability on the company should be removed where there are meaningful and alternative sanctions available which can be imposed on individuals who are involved in the contravention.

Recommendation 5.7

The CLRC recommends that the definition of “officer in default” should be revised to state as follows:

“An officer is 'in default' for the purposes of the provision if he authorises or permits or participates in the contravention.”

Recommendation 5.8

The CLRC recommends that the regulator should be given a general power to initiate civil proceedings on behalf of the company if it appears that it is in the interest of the public to do so. The amount of compensation recovered should first be utilised to reimburse the regulator for all costs incurred in respect of investigations or proceedings in relation to the contravention and second, to compensate aggrieved persons who have suffered loss or damage as a result of the contravention. A criminal action against a director should be permitted even though civil proceedings are underway or have been resolved. In addition, civil proceedings by the company and/or shareholders should be permitted even though the regulator has initiated civil proceedings.

Recommendation 5.9

The CLRC recommends that administrative sanctions in the Companies Act 1965 should be retained but that their use should be best applied for small and relatively insignificant regulatory contraventions.

Recommendation 5.10

The CLRC recommends that section 130 of the Companies Act 1965 should be retained but clarified to state that a person who is disqualified under the section ceases to hold office as a director of a corporation and ceases to be entitled to be directly or indirectly concerned or to take part in the management in Malaysia of a corporation for so long as he shall be disqualified.

Recommendation 5.11

The CLRC recommends that the current position in relation to automatic disqualification should be retained, i.e. that there should be automatic disqualification for:

- (a) conviction of an offence involving fraud or dishonesty;
- (b) being an undischarged bankrupt;
- (c) conviction in relation to offences in connection with the promotion, formation or management of a company or under sections 132 or 303 of the Companies Act 1965.

Recommendation 5.12

The CLRC recommends that a director who has contravened the legislative provisions relating to directors duties may be disqualified upon an application by the regulator.

Recommendation 5.13

The CLRC recommends that the Companies Act 1965 should enable a disqualification order to be made if there is persistent default or contravention of the Act.

Recommendation 5.14

The CLRC recommends that section 130A of the Companies Act 1965 should be clarified to state that a person may be disqualified if within the last five years, the person has been a director of two or more companies when they were wound up in insolvency and that the manner in which the companies were managed, including the director's conduct in relation to the management, business or property of the companies, was wholly or partially responsible for the companies' insolvent liquidation.

Recommendation 5.15

The CLRC recommends that there should be publicity of the persons against whom a disqualification order has been made.

Chapter One

Creating a
Conducive Legal
and Regulatory
Framework for
Businesses

CHAPTER ONE

CREATING A CONDUCTIVE LEGAL AND REGULATORY FRAMEWORK FOR BUSINESSES

1 INTRODUCTION

- 1.01 In this chapter, the CLRC acknowledges the need to distinguish between different types of companies and considers simplification of the rules which have an impact on compliance cost, particularly when these rules affect small companies. While simplification of the rules is a major objective of the corporate law reform programme in general and specifically in the issues considered in Chapter One, the review is also conducted with the aim of ensuring that stakeholders' confidence in the integrity and reliability of corporate information is maintained.
- 1.02 Chapter One considers the basic structure of the corporate legislation, the incorporation process and important concepts that relate to a company, for example the relevance of the objects clause, the doctrine of constructive notice, the ability of private companies to raise capital, the requirement for mandatory audit and the need for company secretaries. Some of these issues have also been dealt with by the Companies (Amendment) Act 2007. While alternative business vehicles in the form of a Limited Liability Partnership structure for Malaysia was identified as an area for review in the "Strategic Framework for the Corporate Law Reform Programme" and CD 7, this issue has been taken up by SSM.¹

¹ On April 1 2008, a CD on LLP was issued by SSM for public consultation. The consultation period ended on 30 June 2008.



2 THE NEED FOR A SINGLE COMPANIES STATUTE AND THE SIMPLIFICATION AND REFINEMENT OF LAW

2.01 The CLRC acknowledges that the blanket application of the companies legislation to all companies, irrespective of size and structure, imposes compliance and administrative burdens on small and closely held companies.² Nevertheless, the CLRC is not persuaded by the argument that small and closely held companies would be better off if administered under a separate piece of legislation that caters to their specific needs.

2.02 The CLRC believes that a single piece of companies' legislation to govern all companies, irrespective of size and structure, will better facilitate business growth and promote a company's natural business progression from small to large without the unnecessary cost of re-incorporation and at the same time avoid transitional problems for companies wanting to expand their businesses.

2.03 On the basis that there should be only a single companies legislation, the CLRC is of the view that there should be a simplification of law to reduce the burden faced by small and closely held companies.

Recommendation 1.1

The CLRC recommends that there should be a single statute that will apply to all companies irrespective of whether the companies are small or large (in terms of ownership structure or economic size, etc.).

² Closely held companies are usually small in membership structure but not necessarily small in economic size.



3 THE DISTINCTION BETWEEN PRIVATE AND PUBLIC COMPANIES

3.01 As stated in CD 7, the CLRC acknowledges that to abandon the private/public distinction will complicate the application and enforcement of company law. The CLRC believes that by abandoning the private/public distinction, it may not be very clear for businesses at which point of time they are entitled to differential treatment for purposes of their statutory obligations, especially during the transitional/growth period of small companies. This would result in an increase in monitoring costs given that there is no definite point of time for any exemptions to their statutory obligations to apply. Thus, the CLRC is not convinced that the private/public distinction should be abandoned.

3.02 However, the CLRC acknowledges that while the present regulatory framework recognises some distinctions between public and private companies in terms of fund-raising, governance and financial reporting, these are not sufficient to address the needs of small, closely held private companies. Thus, the CLRC recommends that the present public/private distinction be retained in general, and that any fund-raising, governance or reporting requirements be looked at specifically and, if necessary, be reformed to suit the needs of small and closely held companies.

Recommendation 1.2

The CLRC recommends that the distinction between public and private companies be retained and that this be used as a basis when simplifying and making company law more conducive to businesses.

4 THE ABILITY OF PRIVATE COMPANIES TO RAISE CAPITAL

- 4.01 The concept of a limited membership (shareholding) is the hallmark of a private company. The CLRC believes that unlike public companies, the members of a private company should be able to determine who should be members of the company. The CLRC is of the view that the present limitation of membership to not more than 50 shareholders should be retained and that there should continue to be a provision that restricts the right of members of a private company to transfer their shares in the Memorandum and Articles of the company.
- 4.02 Where capital raising is concerned, one of the fundamental differences between private and public companies is the prohibition against making an invitation to the public. As private companies continue to grow, additional capital may be required to fund their expansion. Due to the prohibition imposed on private companies against issuing shares to the public, the source of capital for private companies is limited to the contributions by their members. The CLRC believes that this prohibition should be retained as this will be consistent with the rule that members of a private company should be able to determine who should be members of the company.
- 4.03 The CLRC also noted the argument that private companies should be allowed to issue debentures as a means to provide easier access to a wider pool of capital. However, to a certain extent, private companies already have the ability to tap into the capital market particularly through the issuance of debentures (especially the issuance of bonds) to sophisticated investors within the meaning of section 4(6)(b) of the Companies Act 1965. The prior approval of the Securities Commission is required for a proposal for an offer or an invitation in relation to debentures whether by a private or public company. As such, the CLRC is of the view that the issuance of debentures by private companies is already highly regulated with sufficient investor protection mechanisms in place. Thus, the CLRC recommends that instead of deleting section 15(1)(c) and (d) of the Companies Act 1965 from the definition of a private company, any reference to the word "debentures" in the subsections should be deleted.

4.04 In CD 7, the CLRC also deliberated on whether there should be a clarification of what constitutes “an offer to the public”. The CLRC thus recommends the adoption of section 756 of the UK Companies Act 2006.³

Recommendation 1.3

The CLRC recommends that a private company should be defined as one where its Memorandum or Articles of Association:

- (a) provides that the number of its members shall not exceed 50;
- (b) restricts the right of its members to transfer their shares; and
- (c) prohibits an offer or issue of its shares (but not debentures) to the public.

Recommendation 1.4

The CLRC recommends the adoption of the definition of “an offer to the public” in relation to the restriction on public offers by private companies as stated in section 756 of the UK Companies Act 2006.

³ “(1) This section explains what is meant in this Chapter by an offer of securities to the public.
(2) An offer to the public includes an offer to any section of the public, however selected.
(3) An offer is not regarded as an offer to the public if it can properly be regarded, in all the circumstances, as-
(a) not being calculated to result, directly or indirectly, in securities of the company becoming available to persons other than those receiving the offer, or
(b) otherwise being a private concern of the person receiving it and the person making it.
(4) An offer is to be regarded (unless the contrary is proved) as being a private concern of the person receiving it and the person making it if-
(a) it is made only to persons already connected with the company and, where it is made on terms allowing that person to renounce his rights, the rights may only be renounced in favour of another already connected with the company; or
(b) it is an offer to subscribe for securities to be held under an employees' share scheme and, where it is made on terms allowing that person to renounce his rights, the rights may only be renounced in favour of-
(i) another person entitled to hold securities under the scheme, or
(ii) a person already connected with the company.
(5) For the purposes of this section “person already connected with the company” means-
(a) an existing member or employee of the company,
(b) a member of the family of a person who is or was a member or employee of the company,
(c) the widow or widower, or surviving civil partner, of a person who was a member or employee of the company,
(d) an existing debenture holder of the company, or
(e) a trustee (acting in his capacity as such) of a trust of which the principal beneficiary is a person within any of paragraphs (a) to (d).
(6) For the purposes of subsection (5)(b) the members of a person's family are the person's spouse or civil partner and children (including step-children) and their descendants.”

5 AUDIT, FINANCIAL REPORTING AND DISCLOSURE

- 5.01 The present legal framework requires all companies to keep and prepare their accounts in compliance with approved accounting standards and to have the accounts audited. With the exception of exempt private companies, the accounts are then required to be lodged with the Registrar. With regard to the requirement of keeping and preparing the accounts in compliance with approved accounting standards, there are views that the value and usefulness of such an exercise may be insignificant compared to its costs. It has been suggested that the preparation of the financial statement is intended primarily for the protection of shareholders and to a lesser extent, creditors. Therefore, in the case of companies which are owner-managed and do not rely on external financing, the need for such an exercise is less significant.
- 5.02 On the other hand, keeping accounting records and preparing financial statements in compliance with approved accounting standards is important and an integral part of corporate governance as it ensures protection of shareholders' interests. Furthermore, the initiatives by the Malaysian Accounting Standards Board (MASB) in introducing a different set of accounting standards for private entities will address the needs of smaller companies.
- 5.03 In relation to the audit requirement, the CLRC considered the following alternatives:
- (a) audit should be mandatory for all companies; or
 - (b) exemptions from audit should be given to certain types of companies.

- 5.04 The CLRC acknowledges that the reliability of financial statements is increased due to the verification of an independent third party by way of an audit. This is because an audit provides reasonable assurance that the financial statements are free of material misstatements. An audit also promotes accountability and transparency and, arguably, it is a reasonable trade-off for a company to be able to operate with limited liability.
- 5.05 The CLRC also is of the view that in relation to the issue of exemption from audit it is necessary to balance the needs of the company against public interest or public accountability. The question of whether an audit should remain mandatory needs to be considered from the perspective of its necessity and the value of audited accounts to a particular company's shareholders and the public.
- 5.06 Where a company is owner-managed, the necessity and value of audited accounts become less significant. On the other hand, where there exist elements of public interest or public accountability,⁴ the necessity and value of audited accounts would become more significant.
- 5.07 In comparable jurisdictions, one of the compelling reasons to do away with the mandatory audit requirement is the prohibitive costs of carrying out an audit that may be perceived as outweighing the benefits of an audit. The CLRC believes that this is not the case in Malaysia and that the costs of an audit should not be considered in isolation.

⁴ A company is said to have an element of public interest or public accountability if there is a high degree of outside interest in the company from non-management investors or other stakeholders, and if those stakeholders depend primarily on the external financial reporting as their means of obtaining financial information about the company, or if the entity has an essential public service responsibility because of the nature of its operations. In addition, companies that hold assets in a fiduciary capacity for or have obligations or liabilities to a broad group of outsiders such as banks, insurance companies, securities brokers/dealers, pension funds, mutual funds or investment banks are also considered as having an element of public interest or public accountability.

- 5.08 The CLRC is of the view that the present rules on audit are not too burdensome on companies, particularly in relation to the costs of carrying out an audit. The CLRC believes that the mandatory audit rules lend credibility to the financial statements of companies, which in turn supports Malaysia as a choice destination to do business and creates a regulatory environment that promotes accountability and transparency.
- 5.09 This conclusion is supported by the findings of the survey commissioned by the CLRC in ascertaining the value of a statutory audit from the perspective of directors of small-medium sized companies (SMEs).
- 5.10 The directors who responded to the survey are mostly of the view that statutory audits are beneficial, necessary and worthwhile for enhancing transparency, corporate governance and internal control, surpassing the benefit of using such audits for the purposes of taxes and bank financing. They mostly perceived that the benefits of an audit outweigh the costs of carrying out an audit. Contrary to popular belief, the survey also indicates that the concerns over the costs of audit are not as alarming as initially anticipated. The directors who responded to the survey would mostly be willing to carry out audits voluntarily even if the audit requirement is not made mandatory under the Companies Act.
- 5.11 Notwithstanding the recommendation to maintain the obligation that all companies must have their accounts audited, the CLRC is of the view that powers should be given to the regulator to exempt certain types of companies from the audit requirement based on a certain set of criteria, for example number of shareholders, annual turnover below a certain threshold, balance sheet below a certain threshold and number of employees.⁵

⁵ See CD 7, para 5.26-5.30.



Recommendation 1.5

The CLRC recommends the retention of the requirements for all companies to keep accounting records and to prepare financial statements in accordance with the approved accounting standards.

Recommendation 1.6

The CLRC recommends the retention of mandatory audit rules for all companies but the regulator should be given powers to exempt the application of the audit provision for certain types of companies based on certain criteria.

Recommendation 1.7

The CLRC recommends that the present rules in regard to filing of audited accounts be retained.

6 COMPANY SECRETARIES

6.01 At present, every company must appoint at least one company secretary who must be a member of one of the prescribed bodies or a person licensed by the Registrar. There are views that there should not be any statutory requirement that every company must have a company secretary. It is noted that in jurisdictions where the appointment of a specific person is not mandated by the law, the company's statutory obligations would still have to be performed by some person, for example by the directors or their agents. Whilst these functions may have been discharged to an acceptable level of competency, the CLRC is more convinced with the argument that there should be a specific person to carry out these functions to ensure that proper accountability is in place.

6.02 As such, the CLRC is of the view that the better approach is to retain the mandatory appointment of company secretaries as the added value provided by the services of company secretaries will enhance the standard of compliance and corporate governance of companies in general.

6.03 The standard of competency and professionalism within the profession is governed by non-statutory codes, best practices and bye-laws of the respective prescribed bodies. Thus there is no uniform mechanism to monitor the competency and professionalism amongst company secretaries.

6.04 The CLRC is also concerned that the appointment of non-professionally qualified company secretaries could have an adverse effect on the level of compliance and enforcement as well as corporate governance standards. The CLRC is of the view that to ensure that company secretaries remain competent and display a high standard of professionalism, a uniform monitoring mechanism should be introduced.

Recommendation 1.8

The CLRC recommends that the mandatory appointment of company secretaries for all types of companies be retained.

Recommendation 1.9

The CLRC recommends that there should be a register of company secretaries to be managed and controlled by SSM.

7 THE CAPACITY OF A COMPANY TO CONTRACT AND CONSTRUCTIVE NOTICE

A. Company's Capacity

7.01 The objects clauses of a company define the company's capacity and sets the parameters within which the company carries on its commercial activities. Anything done outside the objects clauses is ultra vires and cannot be ratified. The doctrine of ultra vires is viewed as being too rigid as it limits commercial transactions that could legitimately be carried out by companies.

- 7.02 The CLRC is of the view that the argument that the objects clauses and the ultra vires doctrine accord protection to shareholders and creditors is no longer tenable. Shareholders are more concerned with the commercial profitability of a particular transaction than its constitutionality, and creditors are more concerned about the ability of a company to pay debts as and when they fall due.
- 7.03 The CLRC noted that section 20 of the Companies Act 1965 has modified the doctrine of ultra vires and provides protection to third parties dealing with a company. The doctrine of ultra vires is preserved only for the purposes of proceedings by members of a company against any directors or former directors as well as any petition by the Minister to wind up a company.
- 7.04 As such, the CLRC is of the view that there should be a statutory provision expressly conferring on newly formed companies the full capacity of a natural person. Nonetheless, companies may elect or decide to have objects clauses. Existing companies should also be given the opportunity to alter their Memorandum and Articles of Association to have unlimited capacity. However, companies formed for non-profit-making purposes pursuant to section 24 are still required to specify their objects. Thus, section 20 of the Companies Act 1965 should still be retained to deal with companies that are required or have decided to specify their objects. This means that the doctrine of ultra vires should be abolished except in its application pursuant to section 20 of the Companies Act 1965.

Recommendation 1.10

The CLRC recommends that newly formed companies should, unless the company otherwise elects, have the full capacity of a natural person and that existing companies be allowed to alter their Memorandum and Articles of Association to have unlimited capacity.

Recommendation 1.11

The CLRC recommends that companies formed for any purpose referred to in section 24 of the Companies Act 1965 be still required to specify their objects.

Recommendation 1.12

The CLRC recommends that section 20 of the Companies Act 1965 be retained.

B Doctrine of Constructive Notice

7.05 The constructive notice doctrine establishes the general rule that persons dealing with a company are deemed to have notice of what is contained in its public documents, including the Memorandum and Articles of Association and other documents lodged with the Registrar.

7.06 To complement the recommendation that companies be accorded the full capacity of a natural person, the constructive notice doctrine as it applies in relation to objects clauses would no longer be relevant.

7.07 Although it has been recommended that the doctrine of constructive notice be abolished for all public documents lodged by a company with the Registrar, the same should not be applicable to company charges. The CLRC notes that the application of constructive notice of the Register of Charges still serves a commercial purpose particularly in the assessment of risk by third parties intending to provide loan facilities to a company.

Recommendation 1.13

The CLRC recommends the abolishment of the doctrine of constructive notice except when it relates to the Register of Charges.

8 COMPANY FORMATION AND RELATED MATTERS

A. Types of Companies that can be Incorporated

8.01 At present, apart from the private/public distinction, section 14 of the Companies Act 1965 classifies companies based on the nature of liability imposed on members upon winding up. Companies are either limited by shares or guarantee, or have unlimited liability.

8.02 The CLRC recommends the retention of the present classification of companies according to the liability of members and finds such classification sufficient in the present business environment.

Recommendation 1.14

The CLRC recommends that the present classification of companies according to liability of members be retained.

B. Minimum Number of Members and Directors

8.03 With the exception of wholly-owned subsidiaries, the Companies Act 1965 requires a company to have a minimum of two members. Every company must have at least two directors, each of whom must have his principal or only place of residence within Malaysia.

8.04 The CLRC is of the view that the law should allow for the formation of single-member companies as this will spur the spirit of entrepreneurship. This is compatible with the present practice where certain companies are structured such that in substance the entire economic interest and control is vested in one single person through the use of nominee shareholder(s), or where one member owns practically all of the shares and the other member owns only one share so as to not breach the legal requirements imposed. The CLRC recommends that a single member can also be the sole director of a company. A single director must have his principal or only place of residence within Malaysia.

Recommendation 1.15

The CLRC recommends that single-member companies be allowed to be incorporated who can be the director who must be a natural person of full age and who has his principal place of residence within Malaysia.

C. Alternative Business Vehicles

8.05 In December 2003, SSM issued a consultation document proposing the introduction of the Limited Liability Partnership regime (LLP)⁶ as an alternative form of business vehicle. The proposal was intended to complement the existing forms of business vehicles by providing a further choice for businesses to structure their operations to make them more competitive regionally and internationally.

8.06 The CLRC welcomes such initiatives as it may provide an alternative choice of vehicle for business entities.

⁶ On April 1 2008, a CD on LLP was issued by SSM for public consultation. The consultation period ended on 30 June 2008.



9 INCORPORATION AND REGISTRATION OF COMPANIES

A. The Name Search and Reservation Process

9.01 Currently, the Companies Act 1965 requires persons intending to form a company to conduct a name search to determine its availability. If the Registrar is satisfied as to the bona fides of the application, the proposed name will be automatically reserved for a period of three months. During the reservation period, no other company shall be registered under the reserved name or one which too closely resembles the reserved name.

9.02 The CLRC is of the view that the mandatory name reservation process adds an unnecessary procedure prior to incorporation. The use of ICT by SSM would make it possible for the public to have immediate access to a directory of names of registered companies and names which are currently being reserved to ensure that there is no duplication of names.

9.03 However, should incorporators want to reserve a name for a limited period, they should be permitted to do so, but this should be optional and not mandatory. Such name reservation process will address the needs of parties who are interested to protect certain names prior to incorporation. At the same time, the CLRC is of the view that the present reservation period should be shortened.

9.04 Further, the CLRC is of the view that the onus to ensure that the proposed name is not prohibited, undesirable or too similar to an existing company should be placed on the persons who intend to incorporate a company. The CLRC recognises further that there should be clear provisions in the Companies Act 1965 to exonerate the Registrar from liability of a civil action involving passing off.

9.05 Currently, the Registrar has the power to refuse the registration of a name which is undesirable, or one which the Minister has directed the Registrar not to accept for registration, and the power to direct a company to change its name on certain grounds including instances where the name of the company is identical to that of another company, or if in the opinion of the Registrar it closely resembles the name of an existing company at the time of incorporation. The CLRC is of the view that this power should still be retained to complement the proposed recommendation of doing away with the mandatory name reservation process.

Recommendation 1.16

The CLRC recommends that the mandatory name reservation process be done away with, and that the register of reserved names should be made available to the public.

Recommendation 1.17

The CLRC recommends that promoters have the option to reserve a name, for a shorter period.

Recommendation 1.18

The CLRC recommends that clear provisions should be made in the Companies Act 1965 to exonerate the Registrar from liability under any civil action involving passing-off, similar to section 11A(8).

Recommendation 1.19

The CLRC recommends that the Registrar should retain the power to direct a name change.

B. Simplification of the Incorporation Process

9.06 At present, there are various forms and documents that need to be lodged with the Registrar for the purposes of incorporation.

9.07 To simplify a company's incorporation, the CLRC is of the view that the information contained in various documents should be consolidated into a single form. However, certain documents which are currently required to be lodged should still be necessary, for example the company's Memorandum and Articles of Association.

Recommendation 1.20

The CLRC recommends that a single incorporation document in a prescribed form be introduced to simplify the incorporation process.

C. Statutory Declarations

9.08 There are many instances where the Companies Act 1965 requires the making and filing of statutory declarations with the Registrar. The purpose of such statutory declaration is to increase awareness of and act as a caution to a person against making a false statement.

9.09 The CLRC is of the view that the requirement for a statutory declaration should be replaced with a requirement for a statement of compliance. The CLRC believes that the value of a statement of compliance as a precaution against false statements is still intact as section 364 of the Companies Act 1965 provides adequate measures to deter a company or any officer from submitting false and misleading statements to the Registrar without the need for a sworn statement. The Companies (Amendment) Act 2007⁷ has reflected such change but only in relation to documents which are filed or lodged electronically. The CLRC is of the view that this provision should also be extended to documents which are filed or lodged physically.

⁷ New section 11(6A) of the Companies Act 1965.



Recommendation 1.21

The CLRC recommends that the requirement for a statutory declaration be replaced with a requirement for a statement of compliance.

D. Certificate of Incorporation

9.10 Once a company is registered, a certificate of incorporation will be issued together with a company number.

9.11 The CLRC notes that the issuance of certificates of incorporation still serves its purpose as a source of identification and/or as evidence of the formation of companies and recommends its retention.

Recommendation 1.22

The CLRC recommends that the issuance of the certificate of incorporation be retained.

E. Company Seals

9.12 The CLRC notes that the requirement for every company to have a common seal still has its significance in the company's day-to-day operations in view of the requirements of other laws and recommends its retention.

Recommendation 1.23

The CLRC recommends that the requirement for every company to have a common seal be retained.

10. FACILITATING ELECTRONIC INCORPORATION AND ELECTRONIC FILING/LODGEMENT OF DOCUMENTS

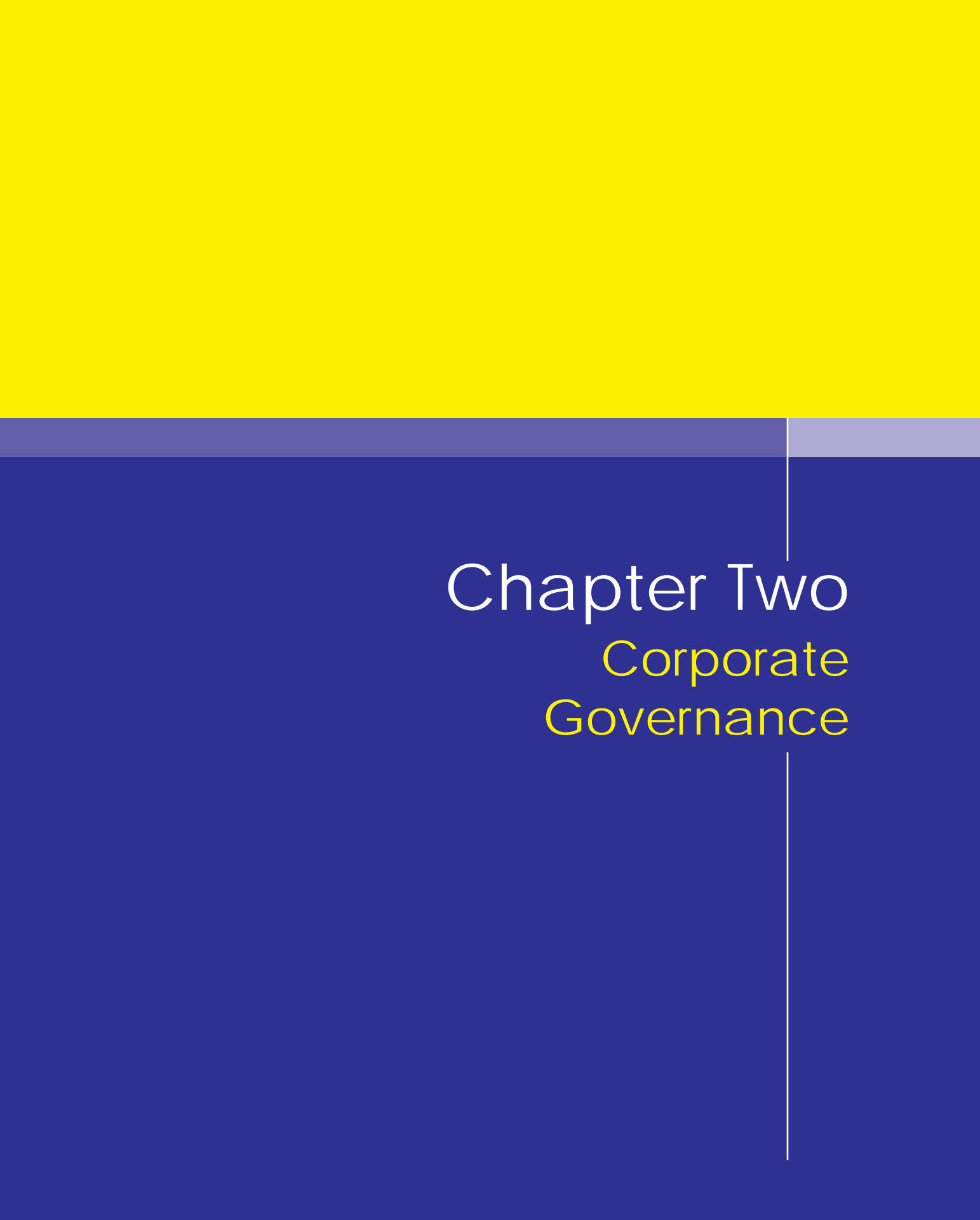
- 10.01 The CLRC acknowledges the importance of electronic filing as a tool to enhance the efficiency of filing or lodgement of documents. To enhance the process of lodgement or filing of documents as well as ensuring its currency, the CLRC recommends that all documents should be filed electronically. However, there should be a transitional period before full migration takes place to allow the public to be familiar with the new system. In CD 7, the CLRC recommended that the provision relating to the attestation of signatures be amended by dis-applying such requirement on documents which are electronically signed. This has already been reflected in the Companies (Amendment) Act 2007.
- 10.02 The review by the CLRC of the provision allowing the Registrar to utilise the electronic service for the issuance of orders, notices, certificates and others to subscribers of the service has also been reflected in the Companies (Amendment) Act 2007. Nevertheless, the CLRC recommends that the definition of “documents” under section 4 of the Companies Act 1965 should be amended to reflect this change.
- 10.03 The CLRC acknowledges that the power of the Registrar to direct a company to lodge a copy of a document when he has reasonable cause to believe such document has been lost or destroyed is equally applicable in an electronic environment. As such, the CLRC is of the view that there is a need to require a person lodging a document electronically to keep a copy of the document and this must be made available to the Registrar, if so required.

10.04 The CLRC also noted the importance of section 11A(8) of the Companies Act 1965 that protects the Registrar from liability against any loss or damage suffered by any person arising from the electronic filing due to any error or omission, provided that the error or omission was made in good faith and in the ordinary course of discharging his duties or occurred as a result of any defect or breakdown in the service or equipment used. The CLRC recommends the retention of this provision.

Recommendation 1.24

To facilitate electronic filing and lodgement of documents, the CLRC recommends that:

- (a) the definition of "documents" under section 4(1) of the Companies Act 1965 be amended accordingly;
- (b) a person lodging a document electronically must keep a copy of the document and this must be made available to the Registrar, if so required; and
- (c) the present arrangement under section 11A(8) be retained, to protect the Registrar from liability against any loss or damage suffered by any person who obtains the documents which were electronically filed or lodged due to any error or omission of whatever nature and howsoever arising if the error or omission was made in good faith and in the ordinary course of the discharge of the Registrar's duties or if it occurred or arose as a result of any defect or breakdown in the service or equipment used for the provision of the service.

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Chapter Two

Corporate Governance

CHAPTER TWO

CORPORATE GOVERNANCE

1. INTRODUCTION

- 1.01 This chapter contains the recommendations of the CLRC on the following areas: Part A - issues relating to meeting processes and procedures and other avenues that may facilitate and encourage shareholders' participation in decision making; Part B - issues relating to mechanisms that ensure and enhance protection of members' rights and remedies; Part C - issues relating to directors' role and responsibilities; Part D - issues relating to auditors' roles and responsibilities; and Part E - issues relating to regulation of substantial property transactions and loans to directors, substantial shareholders and related parties.
- 1.02 In the course of this review, the CLRC referred to international developments as well as the recommendations made by the High Level Finance Committee Report on Corporate Governance 1999 (the CG Report) and considered current initiatives by SSM to implement the recommendations of the CG Report. In the midst of reviewing the relevant areas, the Companies Act 1965 was amended in 2007. As a result, some of the issues and preliminary recommendations highlighted by the CLRC in the various consultation papers released for public consultation have been addressed by the amendments to the Companies Act 1965. There are nonetheless areas which are not dealt with by the amendments and these will be highlighted in this chapter.

PART A - ENGAGEMENT WITH SHAREHOLDERS

2 HOLDING OF ANNUAL GENERAL MEETING

2.01 Annual general meetings (AGMs) remain an important platform for shareholders to question directors generally on the company's business and financial position. This is particularly important in public companies where the company is not owner-managed and where it is not practical for all shareholders to be involved in the management of the company. However, in the case of private companies the mandatory requirement for AGMs is burdensome. On this basis, the CLRC recommends that the Companies Act 1965 should no longer require private companies to hold AGMs. Whilst there are views that an elective regime be adopted for Malaysia, the CLRC is of the view that such a regime will not simplify the law and procedures for private companies.

2.02 As highlighted by CD 3, there were concerns that appropriate safeguards need to be put in place especially in situations where private companies are not owner-managed or where not all shareholders are involved in management. In CD 3 the initial view of the CLRC was that there should either be no shareholding threshold or minimal shareholding threshold to request that an AGM be held for the private company in any one year. While it is important that shareholders should be allowed to request for AGMs to be held, there must be a minimum shareholding requirement to ensure that shareholder(s) requesting for the AGM have sufficient interest in the company to justify the calling of the meeting. However, the shareholding threshold should not be too high so as to unfairly disadvantage minority shareholders. The CLRC is of the view that in a private company, notwithstanding that AGMs are no longer mandatory, the member(s) holding at least 5% of the total voting shares should be given the right to demand for an AGM.

Recommendation 2.1

The CLRC recommends that the Companies Act 1965 should not require a private company to hold annual general meetings.

Recommendation 2.2

The CLRC recommends that in private companies, member(s) holding at least 5% of the total voting shares may demand for an annual general meeting to be held.

A. How to deal with matters which are ordinarily dealt with in an AGM

2.03 Under the no-AGM regime for private companies, the laying of accounts, the appointment of auditors and the appointment of directors will no longer be tied to an AGM:

(a) Circulation of accounts

Although the requirement to circulate the accounts to all shareholders will still be retained, the requirement to lay the accounts before an AGM is not. To give effect to this proposal, it is suggested that the circulation of accounts be tied to a company's financial year-end. It is felt that the present practice of requiring companies to circulate accounts to the shareholders not later than six months after the financial year-end should be retained.

(b) Appointment of auditors

Under the no-AGM regime, the appointment of auditors in private companies⁸ will no longer be linked with the AGM. This means that if an auditor is to be appointed, the appointment is not required to be made at an AGM. The

⁸ This applies where :

(a) a private company is still required to have its accounts audited ; or
(b) if private companies are exempted from audit, where the members require the accounts to be audited.



duration of appointment is no longer from the conclusion of one AGM to the conclusion of the next AGM. The duration of appointment will be in accordance with the terms of appointment, until the auditor is removed by shareholders at a general meeting, or until the auditor resigns.

(c) Appointment and re-election of directors

The appointment and re-election of directors will no longer be made during an AGM but at any general meeting of the private company. The law will provide that a company may appoint a person as a director by resolution passed in general meeting and the duration of the appointment is as stated in the resolution or until the director resigns or is removed. Accordingly, directors may serve as long as the shareholders have no objection.

(d) Lodgement of returns, accounts and reports

In the no-AGM regime, it is proposed that there be a specific time period to file the company's annual returns, accounts and reports to the Registrar. The CLRC is of the opinion that the period for filing of accounts and reports is not later than six months after the end of the financial year unless exempted by the Registrar or the Act.

3. THE USE OF WRITTEN RESOLUTION

A. Unanimity rule

3.01 In CD 3, the CLRC recommended for the amendment of section 152A which currently provides that there must be unanimous shareholder's consent for written resolutions. It was also noted in CD 3 that the UK CLR suggested that the requirement that there must be unanimous consent for written resolutions should be amended. In place of the unanimous consent requirement, the UK CLR suggested that it should be possible for companies to effect a written resolution by the same majority as required for a similar resolution at a meeting (i.e. special resolutions could be passed with a 75% majority and ordinary resolutions by a simple majority), or alternatively to require a high percentage - for example, 90%. As a result, the UK Companies Act 2006 does not require unanimous consent of shareholders for written resolutions.⁹ However, it is to be noted that the written resolution procedure is only applicable for private companies. This is also the position in Singapore and New Zealand. The UK CLR also proposed that all shareholders entitled to vote must be given notice of the proposed written resolution and this has been adopted by the UK Companies Act 2006.

3.02 The CLRC is of the view that the section 152A procedure should be made available only for private companies.¹⁰ The CLRC also recommends that section 152A should be amended to allow a company to pass a written resolution by the same majority as required for the resolution if it was passed at a meeting duly convened. This means that an ordinary resolution is passed by a simple majority of members representing the total voting rights and a special written resolution is passed by a majority of not less than 75% of the total voting rights of eligible members. If passed, a written resolution has the effect as if it was passed by the company in a general meeting or by a meeting of a class of members of the company.

⁹ Section 296(4): "A written resolution is passed when the required majority of eligible members have signified their agreement to it."

¹⁰ See section 288 of the UK Companies Act 2006.



- 3.03 There are concerns from respondents that the passing of a written resolution with less than unanimous consent may compromise minority shareholders' interest. It has been argued that at physical meetings, any shareholder can voice his views and opinions to garner the support from other shareholders, while the procedure for passing a written resolution will deprive shareholders of this opportunity. Respondents also suggested that adequate safeguard should be put in place if the unanimity rule is to be abandoned.
- 3.04 The CLRC is of the view that this concern can be addressed with appropriate safeguards to ensure the interests of minority shareholders are protected. The safeguards can take the following forms:
- requiring private companies to circulate the proposed resolutions to all members who are entitled and eligible to vote;
 - giving members holding at least 5% of the total voting rights the right to request for a meeting to be convened , and
 - providing a period within which the requisite votes to pass the proposed resolution as a written resolution must be obtained, failing which the proposed resolution lapses and is deemed not adopted.
- 3.05 In CD 3, the CLRC was of the view that the notice requirement was an essential right of a member, and in the context of the written resolution procedure, will prevent a resolution from being passed by a majority shareholder without the knowledge of other shareholders.

- 3.06 However, the CLRC also stated in CD3 that the written resolution procedure cannot be applied in certain circumstances, in particular where special notice is required, for instance in cases of the removal of auditors or directors before the expiry of their terms of office. The CLRC noted that this is the position under the UK Companies Act 2006¹¹ and agrees with this approach.
- 3.07 In addition, since it is recommended that the written resolution procedure no longer requires the unanimous consent from shareholders, a time frame needs to be specified for the company to obtain the requisite percentage of votes. The CLRC noted that the UK Companies Act 2006 provides that the period is not more than 28 days or a shorter period as provided in the Articles after the proposed resolution was first circulated. In addition, a member would signify agreement to a written resolution through an authorised document identifying the resolution to which it relates, and the document must be sent to the company in hard copy form or in electronic form. Once a member has signified his agreement to a written resolution, it may not be revoked. The CLRC recommends the adoption of the UK approach.
- 3.08 As to who may propose a written resolution, the CLRC recommends the adoption of section 288(3) of the UK Companies Act 2006 which states that a resolution may be proposed as a written resolution by the directors of a private company, or by the members of a private company. Sections 290-295 of the UK Companies Act 2006 clarify the procedure for the circulation of written resolution proposed by the directors or members of the company. (see Appendix A)

¹¹ See section 288(2) of the UK Companies Act 2006:

“(2) The following may not be passed as a written resolution-

(a) a resolution under section 168 removing a director before the expiration of his period of office;

(b) a resolution under section 510 removing an auditor before the expiration of his term of office.”



3.09 Some of the respondents raised the issue of whether a member may still convene a meeting after the written resolution procedure is adopted by the company to pass a resolution. It is to be noted that even under the present section 152A, a member is not precluded from convening a meeting and that a member may convene an extraordinary general meeting ("EGM") under section 144 or 145 of the Companies Act 1965. The CLRC does not propose to restrict a member's right to convene a physical meeting. It is to be noted that once a resolution is passed by using the written resolution procedure, the decision is as effective and as binding as if the resolution was passed at a meeting which was physically held.

3.10 One question that relates to section 152A is whether section 152A can be used to replace an AGM. Section 152A of the Companies Act 1965 that enables the members to pass a resolution without having to convene a physical meeting has been confusingly used to replace the holding of an AGM, particularly in private companies. With the recommendation that private companies are not required to hold an AGM, this will no longer be an issue.

Recommendation 2.3

The CLRC recommends that section 152A of the Companies Act 1965 be clarified to state that the written resolution procedure is not applicable in certain circumstances where special notice is required and that the written resolution procedures should be available to private companies only.

Recommendation 2.4

The CLRC recommends the removal of the unanimity rule for passing of written resolutions so that written resolutions may be passed by the same majority as required for a similar resolution at a duly convened meeting.

Recommendation 2.5

The CLRC recommends that companies be required to circulate the proposed written resolutions to all members who are entitled and eligible to vote.

Recommendation 2.6

The CLRC recommends that the requisite voting percentage for a written resolution must be obtained within a specified time frame of 28 days after the circulation of the proposed resolution and if the voting percentage is not obtained, the proposed resolution is deemed not carried.

Recommendation 2.7

The CLRC recommends that members holding at least 5% of the total voting rights in a company should be given the right to request for a meeting to be convened.

C. Location of the AGM and the use of ICT in company meetings

3.11 One issue dealt with by the CLRC in CD 3 is the geographical constraint for the holding of an AGM under which an AGM must be held in the state where the registered office of the relevant company is located. This matter has been dealt with by an amendment to the Companies Act 1965.¹² The removal of this constraint greatly facilitates and provides greater flexibility for the decision making process of a company. While there were concerns as to the likelihood of abuse by companies, a company is still under an obligation to ensure that the AGM and any other meetings are convened in such a way so as to give the shareholders a reasonable opportunity to participate. The responses to CD 3 highlighted the need to specify and define the

¹² See section 16 of the Companies (Amendment) Act 2007 substituting section 145A of the Companies Act 1965 with a new provision. Prior to the amendment of the Companies Act 1965, any AGM must be held in the state where the registered office of a company is situated.

“primary venue” for the meeting which should be at a central location and which can be reached with reasonable expenses by members. In CD 3, the CLRC referred to the proposal of Hong Kong's Standing Committee on Company Law Reform (SCCLR) that permitted companies to hold a general meeting at more than one location where the principal venue is the venue specified by the notice of the meeting. The CLRC recommends that this be adopted for Malaysia.

Recommendation 2.8

The CLRC recommends that section 145A of the Companies Act 1965 be clarified to state that a primary venue for a meeting must be specified by the notice of the meeting and that the primary venue should still be in Malaysia.

- 3.12 At the same time, the CLRC is of the view that the advances in ICT should be utilised to facilitate the holding of meetings at more than one location. The CLRC considers that the law should facilitate the holding of a meeting using a technology that uses two-way, real-time communications so as to provide reasonable opportunity for shareholders to participate in the meeting.
- 3.13 There were concerns expressed about the suitability of the proposal to public companies and the need to properly coordinate the conduct and procedures for the meetings. However, as stated in CD 3, the proposal is not mandatory but facilitative in nature and the company is given the discretion to use ICT in conducting meetings. The company still has an obligation to ensure that shareholders are given reasonable opportunity to participate at these meetings. To address any potential abuse or risks of conducting meetings at more than one location, the CLRC proposes that appropriate guidelines should be developed by SSM or the industry.

Recommendation 2.9

The CLRC recommends that the Companies Act 1965 should facilitate the use of any technology that will allow shareholders reasonable opportunity to participate in meetings.

E. Modes of Service

3.14 Unless stated otherwise in a company's Articles of Association, notices of general meetings to a member are to be given personally or by post to the registered address of the member, or in a case where there is no registered address within Malaysia, to an address within Malaysia supplied by the member. The CLRC considered the need to permit expressly in the Companies Act other modes of service including the use of electronic transmission or other means of electronic communication.

3.15 Although there was a general consensus that the use of electronic transmission or other means of electronic communications should be allowed as modes of service, there was concern that adequate safeguards be put in place to ensure that the rights of members to receive notices remain protected. The CLRC is of the view that whilst the Companies Act 1965 should facilitate the use of technology in the decision making process, the company should ensure that adequate safeguards exist to ensure that the convening and holding of a meeting with the assistance of technology does not deprive any members of their right to be informed of and participate in the meeting.

Recommendation 2.10

The CLRC recommends that the Companies Act 1965 should allow for other modes of communication (apart from the requirement that notices of meetings should be given personally or sent by post to shareholders) if shareholders agree.

4 SETTling THE AGENDA: CIRCULATION OF SHAREHOLDERS' PROPOSED RESOLUTIONS AND STATEMENTS

- 4.01 In CD 3, the CLRC considered whether section 151 should be amended in relation to the locus standi given to members based on a specified shareholding or membership, the time frame and the cost issue. The CLRC is of the view that the existing shareholding or membership requirement is sufficient and should be retained. The CLRC recommends the retention of section 151 which allows a requisite number of shareholders (members representing not less than 5% of the total voting rights or 100 shareholders holding shares on which there is an average paid up capital per member of not less than RM500) to circulate notice of any proposed resolution that may be moved at any general meeting and any related statements to shareholders who are entitled to receive notice of an AGM.
- 4.02 However, it is noted that the usefulness of section 151 is limited since a company is not bound to circulate a proposed shareholders' resolution if it is not deposited at least six weeks before a general meeting is convened. The CLRC recommends that the present position in relation to the time frame under section 151(4)(a)(i) be amended. The CLRC is also of the view that the requirement that the requisitionists are to bear the costs of circulating the notice of resolutions should be amended as they constitute significant barrier to shareholders' exercise of their rights.
- 4.03 While the CLRC noted the concern that such costs may deter shareholders from sending in proposed resolutions or statements, there is also the need to ensure that the company is not inundated with trivial, frivolous or vexatious notices or statements. The CLRC is of the view that a requirement that a company is to bear the costs of circulating notices or statements deposited at least four weeks before a general meeting is convened is appropriate to encourage shareholders' activism whilst at the same time provides a safeguard to discourage proposals that may lack substantial value to the company.

Recommendation 2.11

The CLRC recommends the retention of the statutory provision allowing shareholders to circulate any proposed resolution and statement provided that the requisitionists meet the threshold requirements and the document for circulation consists of not more than 1,000 words.

Recommendation 2.12

The CLRC recommends the amendment to section 151(4)(a)(i) of the Companies Act 1965 so that in the case of a requisition requiring notice of a resolution, a company should not be required to give notice of any resolution unless a copy of the requisition signed by the requisitionists is deposited at the registered office of the company not less than four weeks before the meeting.

Recommendation 2.13

The CLRC recommends that the company should be responsible for any costs in sending out the notice of the meeting to members if the company receives the notice in time (if it is deposited not less than four weeks before the meeting).

5 CONDUCTING THE MEETING

A. Appointment of Proxies

5.01 The ability of shareholders to appoint proxies is subject to the statutory limitation that only an advocate, an approved company auditor or persons approved by the Registrar could be appointed. The CLRC however is of the view that the appointment of proxies should not be limited to certain persons only as is found under section 149(1)(b) of the Companies Act 1965, and if there were to be any limitations in terms of persons who may be appointed as proxies, that this should be left to the company

to decide in its Articles of Association. There are concerns that the removal of such limitation will affect the quality of persons appointed as proxies, particularly in respect of their ability to discharge their duties professionally, ethically and in accordance with the law. The CLRC is of the view that the removal of such limitation on the types of persons who can be appointed as a proxy will have the desired effect of encouraging shareholders to vote and hence improve their participation at general meetings.

Recommendation 2.14

The CLRC recommends that section 149(1)(b) of the Companies Act 1965 be deleted.

B. Disclosure of Proxy Voting Information

5.02 The practice of disclosing proxy voting prior to a general meeting has not been prescribed in the Companies Act 1965 although the Malaysian Code on Corporate Governance recommends as best practice the disclosure of information relating to proxy voting prior to the meeting. The CLRC is of the view that although the practice of disclosing proxy voting details prior the general meeting can potentially provide valuable voting information to the shareholders, this should be left as a set of best practices.

Recommendation 2.15

The CLRC recommends against the introduction of any statutory provision requiring the disclosure of proxy voting information in the Companies Act 1965 but proposes that this issue be addressed by way of guidelines and best practices.

C. Voting in Absentia/Postal Voting and Electronic Voting

5.03 The practice of allowing direct absentee voting at meetings of a company is not expressly provided for in the Companies Act 1965 other than section 149 which enables a shareholder to appoint a proxy, representative or attorney to attend and vote in the shareholder's stead. Whilst the CLRC recognises that the Companies Act 1965 should enable any type of voting that will facilitate shareholders' participation in the voting process, the CLRC noted that direct absentee voting/postal voting/electronic voting may create technical and practical difficulties for a company. The CLRC is of the view that direct absentee voting/postal voting/electronic voting should not be made mandatory for companies and this should be addressed by way of guidelines and best practices to prevent possible abuse.

Recommendation 2.16

The CLRC recommends that the Companies Act 1965 be amended to enable direct absentee voting/postal voting/electronic voting. However, this should be facilitative rather than mandatory.

D. Voting by Show of Hands or Poll

5.04 Section 149(1)(a) states that a proxy shall not be entitled to vote except on a poll unless the Articles otherwise provides. However, the Listing Requirements of the Bursa Securities Malaysia Berhad makes it mandatory for public listed companies to include a provision in the Articles of Association allowing proxies to vote by show of hands. There are concerns that voting by show of hands may not represent the true voting position of the company's shareholders as it ignores the number of shares held by each shareholder despite its merit in enabling uncontroversial resolutions to be disposed off quickly.

5.05 The CLRC is of the view that section 149(1)(a) should be amended to allow proxies to vote by show of hands. The method of voting by show of hands should not be prohibited by statute as it provides a method of dealing with uncontroversial resolutions in a convenient, expeditious and inexpensive manner. However, where the member appoints more than one proxy and the voting is to be by show of hands, there could be difficulties in ascertaining which proxy's vote is to be considered and it is better to state that where more than one proxy is appointed, the proxies should not be allowed to vote on a show of hands. Nonetheless, in such cases where there is more than one proxy appointed, it is a matter of best practice for the Chairman to ensure that the members' rights are protected by calling for a vote by poll.

Recommendation 2.17

The CLRC recommends that voting by show of hands should not be prohibited by statute, but neither should it be made mandatory. Where proxy voting is concerned, proxies should be allowed to vote by show of hands but where a member appoints more than one proxy, the proxies should not be allowed to vote by a show of hands.

E. Bundling of Proposed Resolutions

5.06 The bundling of proposed resolutions occurs when several proposals are to be voted on together and not as separate items on the agenda. This practice is not prohibited except under section 126 of the Companies Act 1965 in relation to the appointment of directors of public companies. There are concerns that the practice of bundling of proposed resolutions may be used to hide important details and restricts shareholders' opportunity to debate any contentious parts. However, there are views that the practice of bundling proposed resolutions should not be prohibited on proposals which are generic, interdependent and aligned so as to form one single proposal.

Recommendation 2.18

The CLRC recommends that the practice of bundling of proposed resolutions should not be regulated by statutory provisions but should be addressed by way of guidelines and best practices.

F. Role of the Meeting Chair

5.07 The CLRC is of the view that the general functions and duties of the Chairman of a meeting should not be prescribed by law. The necessarily broad language to formulate the functions and duties of the Chairman would make it unsuitable for legislation or could create considerable difficulties or uncertainties in its interpretation. Further, the law of meetings has sufficiently dealt with the issue of the conduct of the Chairman. Nevertheless, this area could be enhanced by way of best practices.

Recommendation 2.19

The CLRC recommends that there should not be any statutory formulation of the general functions and duties of the Chairman of a meeting. Instead, such roles and functions should be set out in non-legislative documents.

6. MEMBERS' RIGHT TO CONVENE AN EGM (SECTION 144) OR TO REQUISITION AN EGM (SECTION 145)

6.01 Section 144 of the Companies Act 1965 confers on shareholders the right to requisition for the convening of an EGM. The right to convene the meeting however is limited only to members holding not less than 10% of the total voting rights. Section 145 of the Companies Act 1965 provides that a meeting may be convened by two or more members holding 10% of the voting rights. It does not confer the same right to a member, who holds more than 10% of the voting rights.

6.02 The CLRC noted that a shareholding threshold is necessary to enable the management to manage the company without any frivolous interference or disruptions to the orderly management and administration of the company. However, the CLRC acknowledges that the 10% threshold may be too high.

6.03 In CD 3, the CLRC recommended that the 10% threshold be lowered to 5%. Section 145 should be amended so that a member, who, either on his own or with other members, holds not less than 5% of the voting rights be conferred the right to convene a meeting.¹³

Recommendation 2.20

The CLRC recommends that section 144 of the Companies Act 1965 be clarified to enable a member or members holding not less than 5% of the total voting rights to requisition a general meeting.

Recommendation 2.21

The CLRC recommends that section 145 of the Companies Act 1965 be amended to allow a member or members, holding not less than 5% of the total voting rights to convene a meeting of the company.

¹³ At the same time, the CLRC is of the view that the section should be redrafted into two separate sections addressing separately the issues of the right to requisition and convene meetings and notice of meeting.



PART B - CLARIFYING AND REFORMULATING THE DIRECTORS' ROLE AND DUTIES

7 DIRECTORS, DIRECTORS' QUALIFICATION, APPOINTMENT, REMOVAL AND COMPENSATION

A. Definition of "Director" and "Shadow Director"

7.01 The recommendation of the CLRC in CD 5 to amend the current definition of the word "director" under section 4 of the Companies Act 1965 is intended to impose the same obligations and duties of a director on a person who is able to give instructions to the board on how it should act and in accordance with whose instructions the board is accustomed to act. There are also situations where a person who has not been appointed as a director or whose appointment is defective acts or continues to act as a director but is not held accountable merely due to the technicalities of the appointment. The current definition under section 4 makes it practically impossible to hold such a person accountable due to the requirement that the whole of the board must be accustomed to act in accordance with the direction or instruction of the person. As stated in CD 5, the CLRC recommends that section 4 should be amended by adding the words "the majority of the board of directors" to the present definition. The proposed amended definition should be as follows:-

"any person occupying the position of a director of a corporation by whatever name called and includes a person in accordance with whose direction or instructions the majority of the board of directors of a corporation is accustomed to act and an alternate or substitute director".

7.02 Although there are concerns that this may cause inconvenience to holding companies, the CLRC reiterates its view in CD 3 that the mere fact that there is a holding-subsidary relationship does not make the holding company automatically liable as a shadow director as what is required is that there must be a pattern of conduct where the majority of the board is accustomed to act in accordance with the instructions of the person alleged to be the shadow director.

7.03 The CLRC is of the view that there should not be a separate statutory definition for the term "shadow director" since the definition of directors under section 4 effectively encompasses shadow directors.

Recommendation 2.22

The CLRC recommends that section 4 of the Companies Act 1965 should be amended by adding the words "the majority of the board of directors" to the present definition. The proposed amended definition would read as follows:-

"any person occupying the position of a director of a corporation by whatever name called and includes a person in accordance with whose direction or instructions the majority of the board of directors of a corporation is accustomed to act and an alternate or substitute director".

B. Shareholding Requirement, Age Qualification and Residency

7.04 Where the Articles requires a director to hold a specified shareholding to qualify to be appointed as a director, section 124 of the Companies Act 1965 provides that the shareholding must be acquired within two months of the appointment. The CLRC noted that the section does not make it mandatory for a company to impose any share qualification requirement as this is left to be decided by each company and the CLRC does not propose to make share qualification compulsory. As such, the CLRC retains its recommendation to delete section 124 so that this issue is left to be dealt with by the Articles and not to be prescribed by legislation.

- 7.05 In CD 5, the CLRC recommended the deletion of section 129 of the Companies Act 1965 which requires the annual reappointment of a director of a public listed company who has reached the age of 70 years and a vote of not less than three-fourths at the general meeting. The CLRC is of the view that the recommendation be retained as the criterion for appointment should be based on the ability of the director to carry out his role and functions competently irrespective of the age of the director.
- 7.06 The CLRC also recommends that section 122(2) of the Companies Act 1965 be amended to clarify that a person shall have attained the minimum age of not less than 18 years before appointment as a director of a company.

Recommendation 2.23

The CLRC recommends the deletion of section 124 and section 129 of the Companies Act 1965 and the amendment of section 122(2) of the Companies Act 1965 to clearly specify 18 as the minimum age for a person to be appointed as a director.

C. Residency Qualification

- 7.07 In CD 5, the CLRC proposed that the residency requirement be retained. Despite views that this is a cost barrier to foreign investment, the CLRC is of the view that the residency requirement is necessary for enforcement purposes. Therefore, the CLRC has recommended retaining this requirement. Nonetheless, in view of the recommendation for a “one member, one director” company, the residency requirement is to apply to at least one director of the company.

Recommendation 2.24

The CLRC recommends the retention of the residency requirement but in view of the recommendation for a “one member, one director” company, the CLRC recommends that the residency requirement should apply to at least one director of the company.

D. Individual Voting for Appointment of Directors

7.08 The CLRC has recommended in CD 5 to retain section 126 where the resolution to appoint each director of a public company must be voted on separately as this will promote democracy in the election process of directors. Section 126 however provides for the procedure if the resolutions are to be bundled and voted on jointly. The CLRC maintains its recommendation in CD 5 that this section should only be applicable to public companies.

Recommendation 2.25

The CLRC recommends the retention of section 126 of the Companies Act 1965 that requires the resolution to appoint a director of a public company to be voted on individually.

E. Removal of Directors

7.09 In CD 5, the questions raised in relation to section 128 were:

- whether section 128 should be extended to private companies, and
- whether section 128(2) requires special notice to be given for the removal of a director of a company even if the director is to be removed not at a general meeting but in accordance with the Articles of Association.¹⁴

¹⁴ An example is where shareholders holding certain number of shareholding may request in writing for a director to resign.



7.10 In the case of a director of a public company, the general meeting has the authority to remove the director by passing a simple resolution notwithstanding any provision to the contrary in the Articles or any other method of removal as set out in the Articles. Generally the respondents agreed that the provision for removal of a director in a public company under section 128 should be retained. The CLRC is of the view that the section should not be applied to a private company. Even in jurisdictions which allow the director of a private company to be removed by shareholders at general meeting, the applicability of the statutory provision is subject to the company's constitution. A private company however, is not precluded from incorporating a provision with similar effect in its Articles.

7.11 The amendment to section 128(2) in which the words “under this section” have been removed has led to arguments that a special notice is required to be issued to the company for the removal of a director whether or not the removal is to be made at a general meeting and whether or not the company is a private company. The CLRC is of the view that a special notice to the company should only be required in the case of the removal of a director of a public company in accordance with section 128.

Recommendation 2.26

The CLRC recommends that the right of the shareholders at a general meeting to remove a director (as reflected in section 128 of the Companies Act 1965) should be made applicable to public companies only and should not be extended to private companies.

Recommendation 2.27

The CLRC recommends that section 128(2) of the Companies Act 1965 be amended to state that where a director of a public company is to be removed, special notice is required only when the director is to be removed in accordance with section 128 of the Companies Act 1965.

F. Resignation of Directors

7.12 Every company has to file a Form 49 setting out the particulars of its directors, managers and secretaries and any changes thereto to SSM. However, the CLRC noted that some companies have failed to file Form 49 when a director resigned. To resolve the problem faced by directors who have resigned from the company but no notification was made to the regulator, i.e. SSM, the CLRC had recommended in CD 5 the introduction of a provision to enable a person who has resigned as a director to give notice of his resignation to SSM, provided the company has failed to lodge Form 49 within the stipulated period. However, views have been expressed that the director's right to lodge a notice of resignation should not be qualified by the requirement that the company has failed to do so within the stipulated period. In view of this, the CLRC is revising its recommendation in CD 5 so that notice of the resignation of a director may be made by the resigning director himself and the director may give such notice immediately, provided that by such resignation the company is not then in breach of the law. This means that the resignation letter is effective and should be considered by SSM as a change to Form 49. However, the current position that a director shall not resign if the resignation has the effect of reducing the number of directors to less than two persons under section 122(6) shall be retained with modification in view of the recommendation that there can be a "one-director" company.

7.13 Views have also been expressed that the recommendation is not viable unless SSM comes up with a proper procedure to ensure that the resignation of a director is genuine and bona fide (to prevent fraud), done in accordance with the provisions of the Articles of the company or any applicable written agreement and did not contravene section 122(6). However, the CLRC is of the view that the regulatory authorities should not have the obligation of or be involved in ascertaining the validity

of the resignation as this is an internal matter that should be resolved by the company. The submission of the notice will provide some protection to directors against allegations of involvement in future contravention of the law by the company. However, the resignation of a director does not absolve him from any existing liability for contravention which occurred while he was still a director of the company.

Recommendation 2.28

The CLRC recommends that a resigning director should have the right to lodge his notice of resignation to the Registrar at any time after notice of his resignation has been communicated to the company. This right however is subject to the requirement that there should be at least one director of a company at any one time.

G. Directors' Compensation

7.14 The Articles of a company often provides that the directors' remuneration should be determined by the shareholders at the general meeting. As such in CD 5, the CLRC recommended the introduction of a statutory provision that a director's remuneration is to be determined by the shareholders at the general meeting. This will ensure transparency and promote accountability of directors. The recommendation to require shareholders to vote on the remuneration of directors only applies in the case of a public company. The CLRC also retains its recommendation in CD 5 to define "remuneration" in the legislation.

7.15 The CLRC has also recommended the inclusion of a provision to allow shareholders a statutory right to inspect directors' contracts of service. Nonetheless, there are views that such a provision may give rise to abuse as it would enable any shareholder to inspect the directors' contract of service and this can be burdensome to the company. Hence, some of the respondents suggested that the right to inspect be

restricted to members who hold 5% or more of the shares in the company. This threshold will ensure that the inspection rights will not be abused by every shareholder or member of a company. The CLRC noted that the UK Companies Act 2006, does not specify any minimum shareholding or number of members as a requirement for the exercise of the inspection rights but the CLRC does not recommend this approach.

Recommendation 2.29

The CLRC recommends the introduction of a statutory provision that requires the remuneration of directors of public companies to be approved specifically by shareholders at a general meeting. Shareholders and members of a company should be given inspection rights of the directors' contracts of service if requested by (a) members with not less than 5% shareholding or (b) at least 100 members who are entitled to vote at a general meeting.

H. Payment for Loss of Office

7.16 The CLRC is of the view that section 137 which relates to payment to directors for loss of office should be amended to require the same to be disclosed to and approved by the shareholders of the company. However, as stated in CD 5, the CLRC recommends amending section 137 to disallow any interested directors who are also shareholders or persons connected to them to vote in the meeting to decide on the proposed payment to be made in relation to section 137. In CD 5 the CLRC also referred to section 163D of the Hong Kong Companies Ordinance. However, the requirement for disinterested shareholders votes should only be confined to public companies.

7.17 The CLRC also noted that the intent of section 137 may be circumvented by the use of interposed entities where a subsidiary company could be used to provide compensation for loss of office of the directors of its holding company. The CLRC has recommended that the requirement for shareholders' approval should apply in this situation so that the payment must also be approved by the shareholders of the holding company in addition to the shareholders of the subsidiary company.

Recommendation 2.30

The CLRC recommends the retention of section 137 of the Companies Act 1965 with the amendment that the compensation for loss of office for a public company shall be approved by disinterested shareholders.

Recommendation 2.31

The CLRC recommends that where a subsidiary is going to make a payment to its director (whether or not that director is also a director of its holding company) pursuant to section 137 of the Companies Act 1965, that payment should be approved by the shareholders of the holding company in addition to the shareholders of the subsidiary company.

8. CLARIFYING THE ROLE AND FUNCTIONS OF COMPANY DIRECTORS AND THE BOARD OF DIRECTORS

8.01 One of the issues raised in CD 5 relates to the board's autonomy to manage the business of the company as provided under Article 73 of Table A, Fourth Schedule of the Companies Act. The CLRC is of the view that legislation such as the Companies Act may play a significant role in educating the board as to their responsibilities to monitor the management of a company. There should be a general statement in the Companies Act that the board's role and function is to manage the affairs of the company. This has been dealt with by the Companies (Amendment) Act 2007.

9. DIRECTORS' DUTY OF CARE, SKILL AND DILIGENCE AND ENACTING A BUSINESS JUDGMENT RULE

9.01 The recommendations of the CLRC in CD 5 in relation to directors' duty of care, skill and diligence and the business judgment rule have been dealt with by the Companies (Amendment) Act 2007. The CLRC is of the view that the newly introduced statutory provisions on duty of care, skill and diligence (section 132(1A)) and the business judgment rule (section 132(1B)) will ensure accountability whilst providing directors with sufficient protection to better manage companies. Codification of the duty of care, skill and diligence will clarify the standard of care that should be applicable to directors. As stated in CD 5, "[T]his approach proposes that the actual knowledge and experience of a director be taken into consideration as an addition to the minimum standard. This approach will not enable directors, who lack the necessary skill and experience, to use this as a defence. This approach will also encourage directors not to become or remain passive".

9.02 The Companies Act 1965 now contains statutory provisions that empower directors of companies:

- to delegate their powers to others subject to reasonable supervision by the board (section 132(1F));
- to rely on information given by employees or professional advisors or other directors or directors' committees, provided such information is made in good faith and the director concerned has made proper inquiry on the accuracy of such information before relying on it (section 132(1C)).

While there are companies which are owner-managed, it is also a common practice that the affairs of a company are sometimes managed by the management under the supervision of the board. The day-to-day operations may be left to the employees and others including external parties such as professional advisors.

Directors will have to rely on information given by these parties in making corporate decisions. In view of this practice, the CLRC is of the view that the new statutory provisions as introduced by the Companies (Amendment) Act 2007 will clarify the rights of directors to delegate their powers to others and to rely on advice and any reliable information provided by the delegate. The new statutory provisions also clarify the directors' responsibility to ascertain the accuracy of such advice and information before making any decision relating to the company's affairs.

- 9.03 In addition, the business judgment rule has also been codified in section 132(1B). The fundamental purpose of the business judgement rule is to provide directors with a defence in the exercise of their duties. The immunity, however, applies only to directors who have made a business judgment based on good faith or for a proper purpose or who have acted on an informed basis without any conflict of interest and the decision was made in the interest of the company.

10. CLARIFYING AND REFORMULATING DIRECTORS' FIDUCIARY DUTIES

A. Relationship between a Company and its Creditors and Employees

- 10.01 There were views from respondents to CD 5 that Malaysia should adopt the recent amendment under the UK Companies Act 2006 which sees the inclusion of section 172. The section provides that a director, in fulfilling his duties to promote the success of the company for the benefit of its members must consider, inter alia, the interests of the company's employees, the creditors of the company and the impact of the company's operations on the community and the environment.

10.02 Whilst the CLRC supports the proposition that a company must be a good corporate citizen and for its long term sustainability, a company must foster a relationship with its stakeholders, the CLRC is of the view that social obligations of the company should not be incorporated in the Companies Act 1965.¹⁵ Corporate social responsibility should be dealt with by non-statutory guidelines.¹⁶

Recommendation 2.32

The CLRC recommends against the codification of obligations of corporate social responsibility (i.e., the relationship between a company and its creditors and employees) under the Companies Act 1965.

B. Directors' duty of loyalty

10.03 In CD 5, the CLRC made several recommendations to clarify and codify directors' duty of loyalty which comprises the duty to exercise powers in good faith and in the best interest of the company as well as the duty to avoid conflict of interest. The recommendations of the CLRC in CD 5 have been dealt with by the Companies (Amendment) Act 2007. For clarity, the scope of duty of loyalty proposed by the CLRC and now found in the Companies Act 1965 is as follows:

- (a) The duty to act honestly as stated under the former section 132(1) of the Companies Act 1965 has been replaced with an amended section 132(1) where there is an express statement requiring a director to act in the best interest of the company and to use his powers for a proper purpose.

¹⁵ The majority of the responses agreed with the recommendation, noting that creditors and employees protections are sufficiently provided for under sections 292, 303, 304 and 305 and paragraph 7 of the Third Schedule of the Companies Act 1965 and in other legislations such as the Contracts Act, the Employment Act and as well as common law practices.

¹⁶ Bursa Malaysia has introduced the Corporate Social Responsibility (CSR) Framework for Malaysian Public Listed Companies whilst the Securities Commission has included the CSR as part of its corporate governance programme.

(b) A director of a company must avoid a situation in which he has, or will have, a direct or indirect interest that conflicts, or possibly may conflict, with the interests of the company (section 132(2)). Thus a director of a company must not:

- misuse corporate information, property or corporate opportunity;
- engage in business in competition with the company;
- take any benefit from a third party;
- gain advantage (whether direct or indirect) for himself or cause detriment to the company.

However, a company director will not be held liable if there is approval or ratification of the conflict of interest by the appropriate organ of the company, i.e. the shareholders at general meeting.

(c) The primary duty of a director is to act in the best interest of the company that he has been appointed to (section 132(1E)).

11. EXEMPTION AND INDEMNIFICATION OF DIRECTORS' AND OFFICERS' LIABILITY

11.01 Section 140(1) voids any provision whether it is contained in the company's Articles or any contract with the company that has the effect of exempting or indemnifying any officer or auditor of the company in respect of his liability which arises by virtue of that officer or auditor having breached his duty to his company. The CLRC feels that section 140(1) should be preserved as the intention of the section is to prevent an officer or auditor from being exempted from any liability as a result of a breach of duty in advance of the occurrence of such breach.

- 11.02 Under section 140(2) an indemnity is only available to a director, officer or auditor if at the end of a trial, he won the suit or was acquitted. Since a trial takes a long time to complete and may be too costly, some jurisdictions allow the giving of a loan or an advance against the cost of defending the action provided that the amount is repaid to the company if the director's or officer's case is not successful.¹⁷
- 11.03 Whilst the CLRC acknowledges that indemnity should be given to directors, officers or auditors of the company for costs of defending legal actions arising from the directors', officers' or auditors' conduct, an advance should not be possible if the legal action involves potential breach of directors', officers' or auditors' duties to the company. Therefore, the CLRC reiterates its recommendation in CD 5 that a company may be allowed to provide an indemnity for any cost of defending legal proceedings, only when the directors, officers or auditors are successful in their cases. However, the CLRC recommends that section 140(2) should be clarified to state that an indemnity may be given for the purpose of defraying the costs of defending a legal action that has been commenced by a third party (a party other than the company).
- 11.04 In CD 5 another issue that was raised was whether an insurance contract taken by the company is void under section 140. In deciding whether or not to recommend allowing the insurance coverage to cover the liability of directors or officers or auditors, the CLRC was mindful of the personal liability issue as imposed by other statutes, the lengthy process, and the cost of legal proceedings in Malaysia. Nonetheless, an insurance purchased and maintained by a company for its directors or officers or auditors in relation to any potential breach of duty owed towards the company has the effect of exonerating the directors or officers or auditors for any

¹⁷ See section 199A(2) of the Australian Corporations Act 2001.



liability towards the company and undermines the principle that directors or officers or auditors are accountable to the company. However, as stated in the preceding paragraph, third party claims may be insurable by the company.

Recommendation 2.33

The CLRC recommends the retention of section 140(1) of the Companies Act 1965.

Recommendation 2.34

The CLRC recommends that a company be allowed to provide indemnity for any costs incurred by a director, officer or auditor in defending legal proceedings, whether civil or criminal, only when the director, officer or auditor is successful (whether by a judgment in his favour, an acquittal or by a discontinuance).

Recommendation 2.35

The CLRC recommends that a company should not be allowed to purchase or maintain insurance for directors, officers or auditors in relation to liability owed towards the company.

Recommendation 2.36

The CLRC recommends that section 140 of the Companies Act 1965 should be clarified to allow a company to purchase or maintain insurance or to indemnify its officer or director or auditor for cost, expenses and liability incurred by that officer or director or auditor in defending an action commenced by a third party (the third party being a person other than the company).

Recommendation 2.37

The CLRC recommends that any insurance or indemnification that is allowed to be taken by the company for its directors or officers or auditors (as stated in recommendation 2.36) will have to be disclosed to shareholders.

PART C - MEMBERS' RIGHTS AND REMEDIES

12. THE OPPRESSION REMEDY UNDER SECTION 181

12.01 Section 181 is an important statutory provision that enables members and debenture holders to obtain redress where there is oppressive conduct in relation to the conduct of the company's affairs. In CD 6, the CLRC highlighted the need to clarify the wording of the section to clearly show that the remedy is available where the effect of the conduct complained of persists at the time the application was made. Thus the CLRC retains this recommendation and suggests a rewording of the present section 181 to follow the provisions under section 232 of the Australian Corporations Act 2001 as replicated below:

"The Court may make an order under section 233 if:

- (a) the conduct of a company's affairs; or
- (b) an actual or proposed act or omission by or on behalf of a company; or
- (c) a resolution, or a proposed resolution, of members or a class of members of a company;

is either:

- (d) contrary to the interests of the members as a whole; or
- (e) oppressive to, unfairly prejudicial to, or unfairly discriminatory against, a member or members whether in that capacity or in any other capacity."

12.02 Section 181 currently allows debenture holders and members of the company to initiate an action under the section. In CD 6, the CLRC sought views on whether the categories of person who should be given locus standi to bring an application under section 181 should be expanded. The CLRC sought views whether the following persons, i.e., former members, beneficial owners of shares, directors, former directors and/or the regulator should be given the right to bring an application under section 181.

12.03 As noted in *Owen Sim Liang Khui v Piasau Jaya Sdn Bhd*,¹⁸ it is not right for a company to assert that a person has no locus standi when it is the company which had deprived the person of membership and it is this conduct which is alleged to be oppressive. In this situation, a former member who has been deprived of membership should be given locus standi. The CLRC does not intend that all former members should be given locus standi but that this should only be given in limited circumstances as was envisaged in Owen's case. While there is support for the UK Law Commission's view as discussed in CD 6 that former members have alternative remedies and therefore should not be given the locus standi under section 181, the CLRC endorses the view of the majority that former member simpliciter should not be given locus standi but that a former member should be allowed to petition under section 181 if the oppression relates to the circumstances in which he ceased to become a member. Where beneficial owners of shares are concerned, they should be given the right to bring an action under section 181 only where their membership has yet to be perfected. This reflects the dicta in *Owen Sim Liang Khui v Piasau Jaya Sdn Bhd*.¹⁹

12.04 In CD 6, the CLRC also sought views on whether there should be any restriction in relation to a simultaneous application under sections 181 and 218. Since sections 181 and 218 involve different court procedures, they cannot be combined. However, the right of a petitioner to bring an action under section 181 and at the same time to apply to wind up the company under section 218 should not be restricted.

¹⁸ [1996] 1 MLJ 113.

¹⁹ [1996] 1 MLJ 113. See also *Dr Leela Ratios v Anthony Ratios Domingos Ratios* [1996] 4 CLJ 33.



Recommendation 2.38

The CLRC recommends that section 181 of the Companies Act 1965 should be clarified to state that the remedy thereunder is available where the effect of the conduct complained about persists at the time the application is made.

Recommendation 2.39

The CLRC recommends that section 181 of the Companies Act 1965 should be amended to give standing to, in addition to the existing persons who can bring an action under the oppression provision (i.e., members and debenture holders), the following persons:

- (a) a person who is a former member but only if the oppression relates to the circumstances in which he ceased to be a member.
- (b) a transferee of shares or a person entitled to them by operation of law whose membership has not yet been perfected (i.e., beneficial owner).

13. THE DERIVATIVE ACTION AT COMMON LAW AND UNDER THE COMPANIES ACT 1965

13.01 One of the recommendations of the CLRC is the need to introduce a statutory derivative action which will be able to resolve the difficulties faced by members who want to bring an action on behalf of the company under the common law. The Companies (Amendment) Act 2007²⁰ has already introduced a statutory derivative action which is now provided for under section 181A of the Companies Act 1965. This section allows a petitioner to bring an action, to intervene or defend an action on behalf of a company.

²⁰ This Act came into effect on 15 August 2007.



- 13.02 Nonetheless, there are notable differences between the recommendations of the CLRC in relation to the statutory derivative action and section 181A of the Companies Act 1965. One of the issues deliberated on by the CLRC in CD 6 was whether the common law remedy that allows a member to sue on behalf of the company should be retained. The CLRC received strong support from respondents on the recommendation against the retention of the common law derivative action. Thus, the CLRC strongly recommends that the common law derivative action should be replaced by the statutory derivative action as this approach will provide certainty and clarity to the law.
- 13.03 In CD 6, the CLRC also recommended that members (including former members and beneficial owners) and directors should be given locus standi to bring the statutory derivative action. This is also provided for under section 181A of the Companies Act 1965 where members include a person who is entitled to be registered as a member and a former member if the application relates to circumstances in which the member ceased to be a member. While the CLRC sought views as to whether the regulator should be given locus standi, it is to be noted that section 181A(4)(d) of the Companies Act 1965 enables the Registrar in the case of a declared company under Part IX of the Companies Act 1965 to apply for leave of court to bring a statutory derivative action. Part IX deals with companies which have been declared to be put under investigation by the Minister.
- 13.04 Some of the respondents were of the view that the regulator does not have any interest in the company and therefore should not be given locus standi. However, the CLRC has considered in CD 11 that there is merit in introducing a range of enforcement actions that may be taken by the regulator depending on the severity of a contravention of company law. As such, locus standi should also be given to the regulator where the regulator should be able to exercise its discretion whether or

not such an enforcement action should be taken on behalf of the company where there is a public interest element involved. There were also suggestions that there should be a provision where the court may allow “any person who at the discretion of the court, is a proper person” to make an application under this section. This will enable the court to determine whether it is appropriate based on the circumstances to give a person leave to under section 181A of the Companies Act 1965. The CLRC endorses this view and recommends that apart from the persons currently given locus standi under section 181A of the Companies Act 1965, the section should also provide that the court may allow “any person who at the discretion of the court, is a proper person” to make an application under the section.

- 13.05 In CD 6, the CLRC also sought views on whether the statutory derivative action may be brought by members of a company where the cause of action arose in a related company. The majority view was that the statutory derivative action should not be extended to such situations. In such cases, the appropriate person would be the members of the company concerned and not the members of either the holding or the subsidiary company. Although there could be cases where the facts justify an application by members of a related company this should be allowed on a case by case basis. The court should be able to deal with this situation if the court is given the discretion to allow any person who at the discretion of the court, is a proper person to make an application under this section.
- 13.06 The CLRC has also recommended that certain safeguards be put in place to ensure that the section is not abused. These recommendations have been dealt with by the Companies (Amendment) Act 2007 and are as follows:

- (a) the applicant should give not less than 30 days' notice to the company of his intention to bring the action, unless the court otherwise orders and that the applicant shall initiate proceedings within 30 days of the leave being granted. However, the CLRC reiterates that the time frame should be complied with, unless the court otherwise orders.
- (b) the requirement that the company does not intend to bring the action, that the applicant must have acted in good faith and the application is in best interest of the company and that there is a serious question to be tried (section 181B(4)).

13.07 The CLRC also made several recommendations in relation to costs of the proceedings and indemnity as well as orders that the court may make which are now found in the Companies Act 1965.

Recommendation 2.40

The CLRC recommends that the statutory derivative action should be made applicable to all types of companies.

Recommendation 2.41

The CLRC recommends that the common law derivative action should be replaced by the statutory derivative action.

Recommendation 2.42

The CLRC recommends that the statutory derivative action may be brought by any member or director of the company or any person who at the discretion of the court, is a proper person to make an application under this section.

14. VARIATION OF CLASS RIGHTS

14.01 Section 65 of the Companies Act 1965 provides safeguards to shareholders of a particular class against any changes or variation of their rights. The CLRC is of the view that the section requires clarification. The CLRC retains its recommendations in CD 6 relating to section 65.

Recommendation 2.43

The CLRC recommends that a variation of class rights can be done:

- if written consent is obtained from at least 75% of the shareholders whose rights are to be varied; or
- if a special resolution is passed at a separate class meeting of shareholders whose rights are to be varied.

Recommendation 2.44

The CLRC recommends the class rights should be capable of being entrenched in the Memorandum. However, entrenchment should not be absolute in that those rights can still be varied but only with the unanimous consent of that class of shareholders whose rights are to be varied.

Recommendation 2.45

The CLRC recommends that the present law that the statutory procedure applies only where the company has issued more than one type of shares be retained.

Recommendation 2.46

The CLRC recommends that section 65(6) and (7) of the Companies Act 1965 are to be retained.

Recommendation 2.47

The CLRC recommends that where a company proposes to redeem or cancel preference shares (except in the case of redeemable preference shares), this should be statutorily provided as a variation of the rights of the existing preference shareholders.

15. A MINORITY BUY-OUT RIGHT AND THE CLASS ACTION

15.01 In CD 6, the CLRC was of the view that a minority buy-out right should not be incorporated in the Companies Act 1965. While there is majority support for this recommendation, there was also support for the possibility of introducing an exit clause in the Articles of Association of a private company. There were also views that mediation clauses should be introduced in the Articles of Association of a private company. The CLRC however does not recommend that these be statutorily provided for.

15.02 The CLRC also does not recommend the introduction of a class action remedy under the Companies Act 1965.

Recommendation 2.48

The CLRC recommends against the codification of a compulsory minority buy out provision and against the codification of a class action remedy in the Companies Act 1965.

16. STATUTORY INJUNCTION

16.01 In CD 6, the CLRC recommended the introduction of a statutory injunction to allow the regulatory authority or any aggrieved person to prevent breaches or contravention of the Companies Act. The Companies (Amendment) Act 2007 has introduced section 368A which allows the regulator or any aggrieved person to make an application to court for an injunction to prevent contravention of the Companies Act 1965. The CLRC is of the view that this provision will provide greater protection of members' interest as well as add to the regulator's powers to enforce compliance with the Companies Act 1965.

PART D - AUDITORS' ROLES AND RESPONSIBILITIES

17. INTRODUCTION

17.01 CD 12 was released for public exposure on 26 December 2007 and consultation ended on 21 January 2008. This part contains the recommendations of the CLRC after considering the responses to CD 12.

18. APPOINTMENT, REMOVAL, RESIGNATION AND NON-RENEWAL OF APPOINTMENT OF AUDITORS

18.01 The current law provides that the first auditor may be appointed by the board of directors before the first annual general meeting. However, the shareholders in a general meeting may appoint an auditor if the board does not appoint the auditor.²¹ The auditors may also be appointed by the Registrar where the company fails to do so, provided there is an application in writing made by any member of the company.²² The board also has the authority to appoint an auditor where there is casual vacancy.²³

Recommendation 2.49

The CLRC recommends that the existing requirement as to the appointment of an auditor for both public and private companies should be retained.

²¹ Section 172(1) of the Companies Act 1965: "At any time before the first annual general meeting of a company, the directors of the company may appoint, or (if the directors do not make an appointment) the company at a general meeting may appoint, a person or persons to be the auditor or auditors of the company, and any auditor or auditors so appointed shall, subject to this section, hold office until the conclusion of the first annual general meeting." See section 172(2) of the Companies Act 1965.

²² Section 172(10) of the Companies Act 1965.

²³ Section 172(3): "Subject to subsections (7) and (8), the directors of a company may appoint an approved company auditor to fill any casual vacancy in the office of auditor of the company, but while such a vacancy continues the surviving or continuing auditor or auditors, if any, may act. A casual vacancy occurs due to the death or incapacity of any of the auditors."

18.02 However, in view of the recommendation that private companies need not hold an annual general meeting, changes must be made to the current statutory provisions to de-link the appointment of auditors from the AGM.

Recommendation 2.50

The CLRC recommends that in relation to the duration of appointment of auditors for private companies, the duration be in accordance with the terms of appointment, until the auditor is removed by shareholders at a general meeting or until the auditor resigns.

18.03 Where public companies are concerned, the first auditors may appointed by the board and remain as auditors until the expiration of the first AGM of the company. At the first AGM, the existing auditors may be reappointed or new auditors may be appointed in the place of outgoing auditors. Subsequent auditors are appointed by shareholders at each subsequent AGM.²⁴

Recommendation 2.51

The CLRC recommends that the current statutory provisions under section 172(1) and (2) of the Companies Act 1965 relating to the appointment of auditors should be retained.

18.04 In the case of resignation of auditors, the current statutory provisions under section 172(14) and (15) of the Companies Act 1965 that require the resignation to be effective upon the appointment of a new auditor and only if the resignation is made at the general meeting, should be deleted. Thus, where auditors have sent their resignation notice to the company, the effective date of resignation should be at the end of 21 days from the time the notice is deposited with the company. The

²⁴ A company shall at each annual general meeting of the company appoint a person or persons to be the auditor or auditors of the company, and any auditor or auditors so appointed shall, subject to this section, hold office until the conclusion of the next annual general meeting of the company.

auditors may deposit with the notice a signed requisition calling on the directors of the company forthwith duly to convene an extraordinary general meeting of the company for the purpose of receiving and considering such explanation of the circumstances connected with their resignation as they may wish to place before the meeting. While section 172(15) states that the directors shall call a general meeting as soon as is practicable for the purpose of appointing new auditors, there is no time frame specified within which the directors must call and convene a general meeting. The CLRC is of the view that section 172(15) should also be amended such that the directors must proceed duly within 21 days from the date of the deposit of a notice of resignation with the company to convene a meeting on a day not more than 28 days after the date on which the notice convening the meeting is given. Every director who fails to take all reasonable steps to secure that a meeting is convened within the time frame as mentioned above should be guilty of an offence and liable to a fine.²⁵

Recommendation 2.52

The CLRC recommends that section 172(14) and (15) of the Companies Act 1965 be amended to the following effect. In the case of the resignation of auditors, the effective date of resignation would be at the end of 21 days from the time the notice is deposited with the company. The directors must proceed duly within the 21 days to convene a meeting on a day not more than 28 days after the date on which the notice convening the meeting is given. Every director who fails to take all reasonable steps to secure that a meeting is convened as mentioned above shall be guilty of an offence and liable to a fine.

²⁵ See section 518 of the UK Companies Act 2006.



18.05 While an auditor who is removed from office may submit a written representation to the company and request that the written representation be sent to every member who is entitled to receive notices of meetings, there is no similar provision in the case of an auditor who resigns. The recent Companies (Amendment) Act 2007²⁶ imposes a duty on an auditor of a public listed company who is removed from office, or who resigns, and who sends a written representation to the company, to submit the written representation to the Registrar and Bursa Malaysia Securities Berhad within seven days of the submission of the written representation or resignation to the company. The CLRC is of the view that there is a need for the auditor of a public listed company who has resigned to make the reasons for his resignation known. Furthermore, where the auditor considers that there are no circumstances in connection with his resignation that need to be brought to the attention of members or creditors of the company, a statement to that effect should be made and the company should be required to circulate the statement to the shareholders.

Recommendation 2.53

The CLRC recommends that in the case of the resignation of an auditor of a public listed company, the auditor should be required to submit a resignation statement stating either that there are no circumstances connected with his resignation that need to be brought to the attention of members or creditors of the company, or to set out the circumstances for his resignation. The resignation statement should be submitted to the company and the company should be required to circulate it to shareholders. This duty should be in addition to the duty to inform the regulators upon ceasing to hold office as auditor under section 172A of the Companies Act 1965.

²⁶ Section 19 of the Companies (Amendment) Act 2007 introducing section 172A into the Companies Act 1965.



18.06 In CD 12, the CLRC discussed whether there is a need to codify the mandatory rotation of auditors, i.e. in terms of audit partners or audit firms. The CLRC stated in CD 12 that there are concerns that the long tenure of the auditors of a company may compromise the independence of the auditors especially in the context of the audit of public companies. There are nonetheless best practices that have been developed by the profession as safeguards. In addition, codifying mandatory rotation may not be suitable for Malaysia in the current business environment and as such the CLRC is of the view that there should not be a codification of the mandatory rotation of audit firms and that rules relating to mandatory audit rotation should continue to be a matter of best practice.

Recommendation 2.54

The CLRC recommends against a codification of the mandatory rotation of audit firms and recommends that rules relating to mandatory audit rotation should continue to be a matter of best practice.

18.07 The CLRC also sought views on whether the resignation of the auditor should be subject to the regulator's approval. The majority of the respondents were of the view that the resignation of the auditor should be a matter between the company and the auditor concerned.

19. AUDITORS' RIGHTS AND DUTIES

19.01 In CD 12, the CLRC also deliberated on the rights of auditors to access company information, and the right to attend general meetings and be heard on any part of the business of the meeting to which the audit relates. These rights are very important

to ensure that auditors receive the cooperation required to assess the company's accounts so that they may make an assessment of whether or not the company's accounts have been prepared to reflect a true and fair view of the company's financial position. In addition, the Listing Requirements of Bursa Malaysia Securities Berhad also provide the external auditors with the right to request for an audit committee to be convened to consider any matter that the external auditors believe should be brought to the attention of the board.²⁷ The right to request for a meeting of the board is particularly relevant in view of auditors' duty of care.²⁸ The CLRC is of the view that the existing statutory provisions in the Companies Act 1965 on the above matters, i.e. section 174(4), (5), (7) and section 174A are sufficient to assist auditors in the performance of their duty.

19.02 In addition, since a written resolution procedure has been recommended for private companies (recommendation 2.3) an auditor should be entitled to receive all such communications relating to the resolution. This has been expressly provided for under section 502 of the UK Companies Act 2006.²⁹

²⁷ Paragraph 15.25 Listing Requirements of Bursa Malaysia Securities Berhad 2001.

²⁸ *Daniels v Anderson* (1995) 13 ACLC 614.

²⁹ 502 Auditor's rights in relation to resolutions and meetings

- (1) In relation to a written resolution proposed to be agreed to by a private company, the company's auditor is entitled to receive all such communications relating to the resolution as, by virtue of any provision of Chapter 2 of Part 13 of this Act, are required to be supplied to a member of the company.
- (2) A company's auditor is entitled-
 - (a) to receive all notices of, and other communications relating to, any general meeting which a member of the company is entitled to receive,
 - (b) to attend any general meeting of the company, and
 - (c) to be heard at any general meeting which he attends on any part of the business of the meeting which concerns him as auditor.
- (3) Where the auditor is a firm, the right to attend or be heard at a meeting is exercisable by an individual authorised by the firm in writing to act as its representative at the meeting.

Recommendation 2.55

The CLRC recommends the enactment of a statutory provision giving the auditor the right to be provided all communications relating to any resolutions which the company proposes to pass by way of the written resolution procedure.

19.03 In CD 12, the CLRC discussed the position of common law in relation to auditors' duties. The CLRC also sought views on whether there should be codification of the persons to whom auditors owe a duty of care. The current legislation confines the duty of care owed by auditors to members of the entity to which the auditors report. This is appropriate as it is the members and not any other party, e.g. a creditor, who engages the auditors and remunerates them for their services. Case law has also established that the auditors only have a special relationship with a third party when there is an expressed acceptance of liability by the auditors vis-à-vis the claimant. Identifying by statutory provision the categories of persons to whom auditors owe a duty may be difficult and thus, this should be developed by common law.

Recommendation 2.56

The CLRC recommends against codification of the categories of persons to whom auditors owe a duty of care and recommends that any development should be left to case law on a case to case basis.

Recommendation 2.57

The CLRC recommends the retention of the current regime that relies on statute to state the general duty of auditors to report whether the accounts give a true and fair view of the company's financial position, while relying on best practice and self-regulation to provide guidance on whether the accounts give a true and fair view of the company's financial position.

20. OVERSIGHT OF THE AUDITING PROFESSION

20.01 A common component of the various jurisdictions that have considered auditor oversight is the concept of independent regulation of the auditing profession. In CD 12, the CLRC sought views on the need for the establishment of an oversight body that will be responsible for the inspection of auditors to ensure that they comply with international and domestic auditing and ethical standards and for the investigation and the imposing of proportionate sanctions on errant auditors. There was overwhelming support for such an oversight body.

Recommendation 2.58

The CLRC recommends that an independent Auditing Oversight Body should be established, comprising persons other than members from the professional accounting bodies, such as regulators, investor associations and industry associations. This proposed body should be responsible for the inspection of auditors to ensure that they comply with international and domestic auditing and ethical standards as well as be responsible for the investigation and the imposition of proportionate sanctions on errant auditors. This proposed body will co-exist with professional accounting bodies which would be responsible for the professional functions of the audit profession.

PART E - CORPORATE GOVERNANCE - REVIEW OF PROVISIONS REGULATING SUBSTANTIAL PROPERTY TRANSACTIONS, DISCLOSURE OBLIGATIONS AND LOANS TO DIRECTORS

21. REGULATING SUBSTANTIAL PROPERTY TRANSACTIONS

21.01 In CD 9, the CLRC deliberated on the regulation of substantial property transactions under sections 132C, 132E and 132G of the Companies Act 1965 and the Listing Requirements of Bursa Malaysia Securities Berhad. The recent amendment to the Companies Act 1965 has made changes to the relevant statutory provisions identified above.

21.02 While the amendments are timely, the CLRC is of the view that further improvements and clarification should be made to sections 132C and 132E. While the CLRC agrees that there should be shareholders' approval for transactions coming within sections 132C and 132E, the requirement for disinterested shareholders' voting to approve substantial property transactions should only be applicable to public companies. The CLRC is of the view that extending the requirement for disinterested shareholders' voting to private companies is impractical as these companies are normally dependent on the close involvement of the majority shareholders.

Recommendation 2.59

The CLRC recommends that the requirement for disinterested shareholders' voting to approve substantial property transactions under sections 132C and 132E of the Companies Act 1965 should only be applicable to public companies.

- 21.03 It is also noted that while all the respondents agree with the CLRC's recommendations that there should be a distinction between transactions entered into by public listed and non-public listed companies and private companies, there was mixed response in relation to the threshold suggested by the CLRC for transactions entered into by non-public listed companies and private companies. The CLRC's recommendation in relation to the substantial value of a transaction entered into by a non public listed company or a private company is:
- (a) if the transaction exceeds 10% of the company's assets value and is more than RM50,000; or
 - (b) if the transaction exceeds RM500,000.

Some of the respondents were of the view that a lower threshold of RM250,000 is more appropriate.

- 21.04 Nonetheless, the proposal that the "net assets" test should be adopted and that the net assets are to be determined by reference to the most recent financial statements received unanimous support from the respondents.

Recommendation 2.60

The CLRC recommends that the threshold of substantial value under sections 132C and 132E of the Companies Act 1965 in respect of a transaction in relation to non-public listed companies should be as follows:

- (a) if the transaction exceeds 10% of the company's net assets value and is more than RM50,000; or
- (c) if the transaction exceeds RM250,000,

and that the net assets are to be determined by reference to the most recent financial statements.

21.05 In CD 9, the CLRC also reviewed the effect of a transaction which was entered into in contravention of section 132C or 132E, where the transaction is void. The CLRC is of the view that the transaction should be avoidable and not void if entered into in contravention of either of the sections. The company should be allowed to avoid an arrangement or transaction that has been entered into without shareholders' approval. Nevertheless, ratification should be possible and that if there is ratification, the requirement for disinterested shareholders' voting will apply in the case of a public company. However, the right of the company to avoid the transaction should not be exercisable in certain situations where bona fide third parties are involved.

Recommendation 2.61

The CLRC recommends that a transaction entered into in contravention of section 132C or 132E of the Companies Act 1965 be voidable by the company. The CLRC also recommends that, bona fide third parties must be protected and that a transaction or arrangement entered into without shareholders' approval cannot be avoided by a company in the following instances:

- (a) where restitution of any money or other asset that was the subject matter of the transaction is no longer possible;
- (b) where the company has been indemnified for any loss or damage resulting from the transaction; or
- (c) where rights are acquired in good faith, for value and without actual notice of the contravention by a person who is not a party to the transaction.

22. IDENTIFICATION OF "PERSONS CONNECTED TO DIRECTORS" - REVIEW OF SECTIONS 6A AND 122A OF THE COMPANIES ACT 1965

22.01 In reviewing the statutory provisions on substantial property transactions, the CLRC is of the view that there was a need to clarify certain key phrases that will help clarify and assist in the effective implementation of the statutory provisions that regulate substantial property transactions. These key phrases relate to identifying who would fall within the category of "persons connected to directors", "a body corporate associated with a director" and "controlling interest" under section 122A of the Companies Act 1965. The CLRC retains the recommendations that were made in CD 9 on this issue.

Recommendation 2.62

The CLRC recommends to amend section 122A(2), i.e. the definition of "persons connected to directors" to state:

"In paragraph (1)(a) the members of the director's family are his spouse, parent, child (including adopted child and step child), brother, sister and the spouse of his child, brother or sister."

Recommendation 2.63

The CLRC recommends the definition of "a body corporate associated with a director" be as follows:

"For the purposes of paragraph (1)(b) a body corporate is associated with a director if-

- (a) the body corporate is accustomed or is under an obligation, whether formal or informal, or its majority of directors are accustomed, to act in accordance with the directions, instructions or wishes of that director; or
- (b) that director has a controlling interest in the body corporate; or
- (c) that director or a person connected with him, or that director or persons connected with him, are entitled to exercise, or control the exercise of, not less than 20% of the votes attached to voting shares in the body corporate."

Recommendation 2.64

The CLRC recommends that the meaning of “controlling interest” or the concept of control be defined under section 122A(3)(b) be as follows:

“A person is deemed to have control or have a controlling interest in a body corporate if the person or persons connected to him or the person together with persons connected to him-

- (a) holds more than 50% of the issued share capital of the body corporate; or
- (b) controls more than 50% of the voting power of the body corporate; or
- (c) is able to control the composition of the board of directors of the body corporate.”

22.02 The CLRC also reviewed section 6A of the Companies Act 1965, i.e., what constitutes 'interest in shares' in relation to the disclosure requirements by substantial shareholders to clarify the uncertainties in relation to the extent that a person is deemed to have an interest in shares of a company arising out of section 6A(4)(c) through interposed entities.

Recommendation 2.65

The CLRC recommends that section 6(4) of the Companies Act 1965 be amended to state:

“A person shall be deemed to have an interest in a share where a body corporate has an interest in that share and-

- (a) the body corporate, or a majority of its directors are accustomed, or is under an obligation, whether formal or informal, to act in accordance with the direction, instructions or wishes of that person in relation to that share;
- (b) that person has a controlling interests in the body corporate; or
- (c) that person or the associates of that person or that person and his associates are entitled to exercise or control the exercise of not less than 20% of the votes attached to the voting shares in the body corporate.”

23. LOANS TO DIRECTORS AND PERSONS CONNECTED TO DIRECTORS

23.01 Under the Companies Act 1965, loans to directors or persons connected to directors are prohibited except in the case of exempt private companies, i.e. companies which do not have more than 20 shareholders all of whom are not bodies corporate. The views sought by the CLRC and the CLRC's recommendations relate to whether the total prohibition should be retained and if yes, whether the types of transactions under sections 133 and 133A should be extended to "financial benefits", for example quasi-loans or other credit transactions. The CLRC's recommendation that the section should be retained received majority support from the respondents. There were also views that sections 133 and 133A should be extended to "financial benefits" for example quasi-loans or other credit transactions. While this approach would minimise the incidents of these sections being manipulated, there were also strong views that such an approach would unnecessarily extend the scope of the section. The CLRC agrees with this view.

Recommendation 2.66

The CLRC recommends no changes to the ambit and scope of sections 133 and 133A of the Companies Act 1965. The CLRC also recommends not to extend sections 133 and 133A to "substantial shareholders" or "person connected to shareholders".

24. REVIEW OF SECTION 131 OF THE COMPANIES ACT 1965

24.01 In relation to section 131 of the Companies Act 1965, the CLRC's is of the view that the principle of law embodied in section 131 of the Companies Act 1965 be retained. The CLRC is of the view that a director must disclose his direct or indirect interest in any contract or proposed contract with the company to the board of directors of his

company where there exists a conflict or potential conflict of interest in respect of that contract or proposed contract. In addition, a director should only be made accountable for contravening section 131 if he is aware of the interest and intentionally does not disclose the interest.³⁰ It is only reasonable that a director who unintentionally contravenes section 131 should not be made accountable for his non-disclosure and that section 131 should be clarified on this point.³¹ The CLRC nonetheless is of the view that some modifications be made to section 131 of the Companies Act 1965. These are in relation to the method of declaration of the interest and the consequences of a transaction which is entered into in contravention of section 131 of the Companies Act 1965.

Recommendation 2.67

The CLRC recommends to retain section 131 to the effect that that a director must disclose his direct or indirect interest in any contract or proposed contract with the company to the board of directors of his company where there exists a conflict or potential conflict of interest in respect of that contract or proposed contract, be retained.

Recommendation 2.68

The CLRC recommends that a director should only be made accountable for contravening section 131 if he is aware of the interest and intentionally does not disclose the interest.

Recommendation 2.69

The CLRC recommends that any declaration under of interest under section 131 of the Companies Act 1965 must be made in accordance with any of the following methods:

- (a) at a meeting of the board of directors

³⁰ See *Lim Foo Yong v PP* [1976] 2 MLJ 259 where it was held that no offence is committed if the director could not have reasonably known about the conflict.

³¹ Section 162(3) of the Hong Kong Companies Ordinance expressly provides that a director is not guilty of an offence if he is not aware of the contract that gave rise to the conflict of interest.

- (b) by notice in writing
- (c) by giving a general notice of future conflict of interest pursuant to section 131(4) of the Companies Act 1965.

25. REVIEW OF DISCLOSURE BY SUBSTANTIAL SHAREHOLDER

25.01 In relation to disclosure of shareholding by substantial shareholders, the CLRC is of the view that section 131 of the Companies Act 1965 should be retained. The current threshold of 5% as is currently provided for by section 69D is to be retained as it is the usual practice for countries to peg their threshold percentage between 3 to 5%.³² There is also no necessity to change the current timeline of seven days for giving the required notice to the company pursuant to sections 68E, 69F and 69G of the Companies Act 1965. While some jurisdictions have adopted the rule that require a substantial shareholder to notify his company only where there is a change in the prescribed percentage level of the interest or interests in the voting shares held by the substantial shareholder, the CLRC is of the view that the present provisions is less confusing and will ensure less risk of unintentional non-disclosure due to miscalculations.

Recommendation 2.70

The CLRC recommends:

- (a) to retain the current threshold of 5% as is currently provided for by section 69D
- (b) to retain the current timeline of seven days for giving the required notice to the company pursuant to sections 68E, 69F and 69G of the Companies Act 1965.

Recommendation 2.71

The CLRC recommends that there is no necessity to propose a threshold or de minimis rule for section 69F of the Companies Act 1965.

³² In Australia and Singapore, the threshold is pegged at 5% whilst in the UK it is pegged at 3%..



Appendix A- excerpts from the UK Companies Act 2006

CHAPTER 2

WRITTEN RESOLUTIONS

General provisions about written resolutions

288 Written resolutions of private companies

- (1) In the Companies Acts a “written resolution” means a resolution of a private company proposed and passed in accordance with this Chapter.
- (2) The following may not be passed as a written resolution-
 - (a) a resolution under section 168 removing a director before the expiration of his period of office;
 - (b) a resolution under section 510 removing an auditor before the expiration of his term of office.
- (3) A resolution may be proposed as a written resolution-
 - (a) by the directors of a private company (see section 291), or
 - (b) by the members of a private company (see sections 292 to 295).
- (4) References in enactments passed or made before this Chapter comes into force to-
 - (a) a resolution of a company in general meeting, or
 - (b) a resolution of a meeting of a class of members of the company, have effect as if they included references to a written resolution of the members, or of a class of members, of a private company (as appropriate).
- (5) A written resolution of a private company has effect as if passed (as the case may be)-
 - (a) by the company in general meeting, or
 - (b) by a meeting of a class of members of the company, and references in enactments passed or made before this section comes into force to a meeting at which a resolution is passed or to members voting in favour of a resolution shall be construed accordingly.

289 Eligible members

- (1) In relation to a resolution proposed as a written resolution of a private company, the eligible members are the members who would have been entitled to vote on the resolution on the circulation date of the resolution (see section 290).
- (2) If the persons entitled to vote on a written resolution change during the course of the day that is the circulation date of the resolution, the eligible members are the persons entitled to vote on the resolution at the time that the first copy of the resolution is sent or submitted to a member for his agreement.

Circulation of written resolutions

290 Circulation date

References in this Part to the circulation date of a written resolution are to the date on which copies of it are sent or submitted to members in accordance with this Chapter (or if copies are sent or submitted to members on different days, to the first of those days).

291 Circulation of written resolutions proposed by directors

- (1) This section applies to a resolution proposed as a written resolution by the directors of the company.
- (2) The company must send or submit a copy of the resolution to every eligible member.
- (3) The company must do so-
 - (a) by sending copies at the same time (so far as reasonably practicable) to all eligible members in hard copy form, in electronic form or by means of a website, or

- (b) if it is possible to do so without undue delay, by submitting the same copy to each eligible member in turn (or different copies to each of a number of eligible members in turn),
- or by sending copies to some members in accordance with paragraph (a) and submitting a copy or copies to other members in accordance with paragraph (b).
- (4) The copy of the resolution must be accompanied by a statement informing the member-
 - (a) how to signify agreement to the resolution (see section 296), and
 - (b) as to the date by which the resolution must be passed if it is not to lapse (see section 297).
- (5) In the event of default in complying with this section, an offence is committed by every officer of the company who is in default.
- (6) A person guilty of an offence under this section is liable-
 - (a) on conviction on indictment, to a fine;
 - (b) on summary conviction, to a fine not exceeding the statutory maximum.
- (7) The validity of the resolution, if passed, is not affected by a failure to comply with this section.

292 Members' power to require circulation of written resolution

- (1) The members of a private company may require the company to circulate a resolution that may properly be moved and is proposed to be moved as a written resolution.
- (2) Any resolution may properly be moved as a written resolution unless-
 - (a) it would, if passed, be ineffective (whether by reason of inconsistency with any enactment or the company's constitution or otherwise),
 - (b) it is defamatory of any person, or
 - (c) it is frivolous or vexatious.

- (3) Where the members require a company to circulate a resolution they may require the company to circulate with it a statement of not more than 1,000 words on the subject matter of the resolution.
- (4) A company is required to circulate the resolution and any accompanying statement once it has received requests that it do so from members representing not less than the requisite percentage of the total voting rights of all members entitled to vote on the resolution.
- (5) The "requisite percentage" is 5% or such lower percentage as is specified for this purpose in the company's articles.
- (6) A request-
 - (a) may be in hard copy form or in electronic form,
 - (b) must identify the resolution and any accompanying statement, and
 - (c) must be authenticated by the person or persons making it.

293 Circulation of written resolution proposed by members

- (1) A company that is required under section 292 to circulate a resolution must send or submit to every eligible member-
 - (a) a copy of the resolution, and
 - (b) a copy of any accompanying statement.

This is subject to section 294(2) (deposit or tender of sum in respect of expenses of circulation) and section 295 (application not to circulate members' statement).
- (2) The company must do so-
 - (a) by sending copies at the same time (so far as reasonably practicable) to all eligible members in hard copy form, in electronic form or by means of a website, or
 - (b) if it is possible to do so without undue delay, by submitting the same copy to each eligible member in turn (or different copies to each of a number of eligible members in turn),

or by sending copies to some members in accordance with paragraph (a) and submitting a copy or copies to other members in accordance with paragraph (b).

- (3) The company must send or submit the copies (or, if copies are sent or submitted to members on different days, the first of those copies) not more than 21 days after it becomes subject to the requirement under section 292 to circulate the resolution.
- (4) The copy of the resolution must be accompanied by guidance as to-
 - (a) how to signify agreement to the resolution (see section 296), and
 - (b) the date by which the resolution must be passed if it is not to lapse (see section 297).
- (5) In the event of default in complying with this section, an offence is committed by every officer of the company who is in default.
- (6) A person guilty of an offence under this section is liable-
 - (a) on conviction on indictment, to a fine;
 - (b) on summary conviction, to a fine not exceeding the statutory maximum.
- (7) The validity of the resolution, if passed, is not affected by a failure to comply with this section.

294 Expenses of circulation

- (1) The expenses of the company in complying with section 293 must be paid by the members who requested the circulation of the resolution unless the company resolves otherwise.
- (2) Unless the company has previously so resolved, it is not bound to comply with that section unless there is deposited with or tendered to it a sum reasonably sufficient to meet its expenses in doing so.

295 Application not to circulate members' statement

- (1) A company is not required to circulate a members' statement under section 293 if, on an application by the company or another person who claims to be aggrieved, the court is satisfied that the rights conferred by section 292 and that section are being abused.
- (2) The court may order the members who requested the circulation of the statement to pay the whole or part of the company's costs (in Scotland, expenses) on such an application, even if they are not parties to the application.

Agreeing to written resolutions

296 Procedure for signifying agreement to written resolution

- (1) A member signifies his agreement to a proposed written resolution when the company receives from him (or from someone acting on his behalf) an authenticated document-
 - (a) identifying the resolution to which it relates, and
 - (b) indicating his agreement to the resolution.
- (2) The document must be sent to the company in hard copy form or in electronic form.
- (3) A member's agreement to a written resolution, once signified, may not be revoked.
- (4) A written resolution is passed when the required majority of eligible members have signified their agreement to it.

297 Period for agreeing to written resolution

- (1) A proposed written resolution lapses if it is not passed before the end of-
 - (a) the period specified for this purpose in the company's articles, or
 - (b) if none is specified, the period of 28 days beginning with the circulation date.

- (2) The agreement of a member to a written resolution is ineffective if signified after the expiry of that period.

Supplementary

298 Sending documents relating to written resolutions by electronic means

- (1) Where a company has given an electronic address in any document containing or accompanying a proposed written resolution, it is deemed to have agreed that any document or information relating to that resolution may be sent by electronic means to that address (subject to any conditions or limitations specified in the document).
- (2) In this section “electronic address” means any address or number used for the purposes of sending or receiving documents or information by electronic means.

299 Publication of written resolution on website

- (1) This section applies where a company sends-
 - (a) a written resolution, or
 - (b) a statement relating to a written resolution, to a person by means of a website.
- (2) The resolution or statement is not validly sent for the purposes of this Chapter unless the resolution is available on the website throughout the period beginning with the circulation date and ending on the date on which the resolution lapses under section 297.

300 Relationship between this Chapter and provisions of company's articles

A provision of the articles of a private company is void in so far as it would have the effect that a resolution that is required by or otherwise provided for in an enactment could not be proposed and passed as a written resolution.

Chapter Three

Share Capital and Capital Maintenance

CHAPTER THREE

SHARE CAPITAL AND CAPITAL MAINTENANCE

1. INTRODUCTION

1.01 This chapter relates to the review of the authorised share capital and par value regime and the capital maintenance rules. In reviewing these rules, the CLRC considered the continued relevance of these rules taking into consideration the current law reform exercises in various Commonwealth countries.

PART A: SHARE CAPITAL: NO PAR VALUE ENVIRONMENT

1.02 In CD 2, the CLRC considered the relevance of authorised share capital and the requirement that a company must issue shares with a nominal value, i.e. the par value regime. The authorised share capital and the par value requirements were intended to ensure that shareholders' and creditors' rights are protected. However, as highlighted in CD 2, these requirements are no longer relevant and may be misleading.³³ The CLRC recommended that two archaic concepts in relation to share capital should be abandoned and these are:

- (a) the requirement that a company limited by shares is to state its authorised share capital in the company's Memorandum; and
- (b) the requirement that issued shares are to have a par or nominal value attached to these shares.

³³ Whilst there are views that the abolition of shares with par value could affect shareholders' interests especially in relation to pre-emption rights, voting rights or the assurance of a minimum subscribed capital, the CLRC believes that these concerns are unfounded. As stated in CD 2, the voting rights of shareholders, dividend rights and pre-emption rights are tied up with the amount of shares held by a shareholder and not the value of the shares. The board of directors still have to determine the issue price of all new shares which are to be issued as is currently the practice. The CLRC noted the useful suggestion from respondents that a mechanism to determine the issue price is essential to prevent manipulation and abuse but is of the view that this should not be imposed via statutory provision.

Recommendation 3.1

The CLRC recommends that:

- (a) a company limited by shares be no longer required to state its authorised share capital in the company's Memorandum;
- (b) all shares of a company should no longer have a par value attached to them; and
- (c) the conversion of all shares to shares of no par value should be made mandatory for all companies as at and from the date to be specified as the conversion date.

Recommendation 3.2

The CLRC recommends that companies under the no par value (NPV) regime should be authorised to elect to capitalise their profits without having to increase the number of shares owned by a shareholder (i.e. without any issue of new shares to shareholders), to capitalise their profits coupled with the issue of new shares to shareholders or to consolidate and subdivide the NPV shares.

2. SHARE PREMIUM ACCOUNTS AND CAPITAL REDEMPTION RESERVE

2.01 In a NPV environment, there would not be any requirement to maintain a share premium account. As stated in CD 2, "The share capital account in an NPV environment will be made up of the amount that the shareholders have paid for the shares. That amount will equal the issue price of the NPV share. The amount received by a company for the issue and allotment of NPV shares will be the company's 'contributed capital' account. Further, in an NPV environment a company which has made a profit will still have a retained profit/earning account. The amount standing in the company's retained profit/earning account would remain distributable by way of cash dividend but a company could also decide to capitalise the amount and this will be added to the company's contributed capital."

Recommendation 3.3

The CLRC recommends that companies shall be permitted after the conversion date to issue redeemable preference shares (RPS) without having to maintain a capital redemption reserve when the RPS are redeemed. If the redemption of the RPS is made out of available profits, the company is required to transfer the amount redeemed to the company's contributed capital account.

2.02 The CLRC also considered whether any amount which is standing to the credit of the company's share premium account and capital redemption reserve immediately on or after the conversion date should be included as part of the company's contributed capital.

Recommendation 3.4

The CLRC recommends that the amount standing to the credit of the share premium account and the capital redemption reserve should be capable of being utilised during the transitional period for:

- (a) providing premium payable on the redemption of RPS issued before that date;
- (b) writing off preliminary expenses of the company incurred before that date; and
- (c) writing off expenses incurred, or commissions or brokerages paid or discounts allowed, on or before that date, for any duty, fee or tax payable on or in connection with any issue of the company's shares.

3. ISSUE OF PARTLY PAID SHARES AND LIABILITY FOR UNPAID SHARES

3.01 In CD 2, the CLRC recommended that a company should still be allowed to issue partly paid shares. In a NPV environment, the liability is up to the amount of the issue price remaining unpaid. In cases where there are still existing partly paid shares which were issued under the present par value regime, the liability to pay for the amount remaining unpaid is not extinguished. The unpaid portion will be recognised as the unpaid amount of the issue price.

Recommendation 3.5

The CLRC recommends that the shareholder's liability for any unpaid portion of the issue price of shares should not cease after the conversion date.

3.02 With regard to the adequacy of consideration for shares, the CLRC felt that there should not be any amendments to include any statutory provision that would regulate the type of consideration that may be received by a company when a company issues shares. There should not be a statutory valuation procedure that a company must comply with when a company receives any non-cash consideration in return for issuing its shares. This matter is an internal matter that is to be dealt with by the directors of the company in accordance with their fiduciary duties.

4. COROLLARY CHANGES

4.01 During the review of the law, the CLRC also considered the following sections of the Companies Act 1965:

- (a) section 58 which relates to the power of the company to make payment of certain commissions and prohibition against making payment of other commissions and discounts on the issue of shares;
- (b) section 56(1) that provides companies with the power to make different arrangements for calls and payments for shares;
- (c) section 57 that relates to bearer shares or share warrants; and
- (d) section 56(2) that relates to the provision on reserve capital or reserve liability.

Recommendation 3.6

The CLRC recommends that sections 58, 56(1) and 57 of the Companies Act 1965 should be retained and section 56(2) of the Companies Act 1965 should be abolished.

4.02 The abolition of the par value will require corollary amendments to the Companies Act 1965 such as the removal of the existing section 59, as with the introduction of the NPV regime this section would become redundant. There will also be provisions enacted that are designed to preserve the effect of existing contracts and other instruments that have been executed before the conversion date which refers to the par/nominal value of shares.

4.03 Some of the respondents stated that the transitional period proposed by the CLRC is not adequate for companies to decide whether or not to redeem their redeemable preference shares at a premium. Proposals have been put forward to extend the transitional period from two years to between three and five years to allow companies sufficient time to plan for the utilisation of the share premium account. However, the CLRC feels that the time frame of two years is sufficient time for companies to acquaint themselves with the new regime.

Recommendation 3.7

The CLRC recommends that a time frame of two years be given as a transitional period for all companies to utilise the amount standing to the credit of their share premium account, if any.

PART B: CAPITAL MAINTENANCE RULES AND SHARE CAPITAL: SIMPLIFYING AND STREAMLINING PROVISIONS APPLICABLE TO THE REDUCTION OF CAPITAL, SHARE BUY BACK AND FINANCIAL ASSISTANCE

5. REDUCTION OF CAPITAL - RETENTION OF SECTION 64 AND THE INTRODUCTION OF AN ALTERNATIVE PROCEDURE

5.01 The current section 64 of the Companies Act 1965 provides that a company may only reduce its capital if it has obtained shareholders' approval via a special resolution and that this must be confirmed by the court. As noted in CD 8, the CLRC recommends that this procedure be retained. In addition, the CLRC is of the view that there is merit in introducing an alternative capital reduction procedure which is based on the company's ability to comply with a solvency test and where the company has obtained shareholders' approval. Where the solvency test is concerned, the determination whether or not the company satisfies the solvency test is to be made by the directors, who must make a solvency statement to that effect. There is overwhelming support for the retention of the current section 64 procedure as well as the introduction of an alternative capital reduction procedure.

Recommendation 3.8

The CLRC recommends the retention of section 64 of the Companies Act 1965. The CLRC also recommends the introduction of an alternative procedure for reduction of capital where a solvency test requirement will have to be fulfilled by the company when initiating a reduction of capital exercise. In such a situation, the confirmation of the court should not be required.

5.02 Nonetheless, while the introduction of a solvency test was widely supported, there were two main concerns in relation to the solvency statement: the first relates to the appropriate time frame for determining a company's solvency, and the second relates to the absence of any independent verification of the solvency statement.

5.03 In CD 8, the CLRC recommended the introduction of a "solvency test", which is as follows:

"The company is able to satisfy the solvency test if-

- (a) the company is able to pay its debts as they become due in the normal course of business (cash-flow solvency); and
- (b) the value of the company's assets is greater than the value of its liabilities, including contingent liabilities (balance sheet solvency).

In determining whether the value of the company's assets is not less than the value of its liabilities, the directors:

- (a) must have regard to-
 - (i) the most recent financial statement of the company; and
 - (ii) all other circumstances that, the directors know or ought to know, affect or may affect the value of the company's assets and the value of the company's liabilities, including its contingent liabilities.
- (b) may rely on valuations of assets or estimates of liabilities that are reasonable in the circumstances."

5.04 There were views that a one-year timeline should be included to determine the appropriate time frame similar to the UK and Singapore provisions. The CLRC agrees with this view and recommend that this be adopted in relation to the solvency test.

5.05 There were also views that there should be an auditor's report and/or a statutory declaration to support the solvency statement to ensure its reliability. However, the concern about this proposal is that auditors may not be willing to sign-off on the solvency of the company, thus making the alternative capital reduction procedure not useful. The CLRC is of the view that the criminal liability proposed to be imposed on directors would ensure that the solvency statement will not be taken lightly. The CLRC therefore does not recommend that the company submit an auditor's report to accompany the solvency declaration by the directors.

Recommendation 3.9

The CLRC recommends the introduction of a statutory solvency test, as follows:

"The company is able to satisfy the solvency test if-

- (a) the company is able to pay its debts as they become due in the normal course of business (cash-flow solvency); and
- (b) the value of the company's assets is greater than the value of its liabilities, including contingent liabilities (balance sheet solvency).

In determining whether the value of the company's assets is not less than the value of its liabilities, the directors-

- (a) must have regard to -
 - (i) the most recent financial statement of the company; and
 - (ii) all other circumstances that, the directors know or ought to know, affect or may affect the value of the company's assets and the value of the company's liabilities, including its contingent liabilities.
- (b) may rely on valuations of assets or estimates of liabilities that are reasonable in the circumstances."

The solvency statement must be made by the directors which states-

- (a) that they have formed the opinion that, as regards the company's situation at the date of the statement, there is no ground on which the company could then be found to be unable to pay its debts; and
- (b) that they have formed the opinion-
 - (i) if it is intended to commence winding up of the company within the period of 12 months immediately following the date of the statement, that the company will be able to pay its debts in full within the period of 12 months beginning with the commencement of the winding up; or
 - (ii) if it is not intended so to commence winding up, that the company will be able to pay its debts as they fall due during the period of 12 months immediately following the date of the statement.

Recommendation 3.10

The CLRC recommends the introduction of a provision to hold any director criminally liable for any false declaration made regarding the solvency status of the company.

5.06 In CD 8, the CLRC had recommended that for a reduction of capital with a solvency statement, the creditors of the company should be allowed to challenge the reduction in court and to object to the reduction. To ensure that there is no abuse of process and to balance this with the need to ensure that creditors' interests are protected, several measures were recommended. One of the measures is the imposition of liability on any creditor who makes any challenges without having any credible grounds or reason to do so. Such creditor will be liable to costs incurred

in the filing of such a challenge.³⁴ This is supported by a majority of the respondents. The CLRC thus retains this recommendation. While there were suggestions that the CLRC consider clarifying what are reasonable grounds, the CLRC is of the view that this should be left to the court to decide on a case-to-case basis. There were also views that the current procedure under the existing section 64(2)(b) of the Companies Act 1965 that provides for the method of settling a list of creditors should be included. The CLRC is of the view that such a method is required and agrees to this suggestion, hence recommends that a provision on arriving at the list of creditors be included as part of the capital reduction provisions.

5.07 In CD 8, the CLRC also stated that requirements for publicity are essential to enable creditors to be informed of the proposal for reduction of capital. In addition, an appropriate time frame should be specified to facilitate any challenges that may be made by the creditors on the proposal to reduce a company's capital. Under the UK CLR proposal, a time frame of four weeks is given after the special resolution is passed to enable objections to be made. The CLRC recommends that the same time frame be given under the Companies Act 1965.

5.08 There is also majority support for the recommendation in CD 8 that the grounds for this challenge should be specified, i.e. where the creditors have not been offered security for the debts or any other safeguards, or that the company does not have sufficient assets. Thus, the CLRC retains this recommendation.

³⁴ Section 7A(6) of the Singapore Companies Act reads:

"A director of a company who makes a solvency statement without having reasonable grounds for the opinions expressed in it shall be guilty of an offence and shall be liable on conviction to a fine not exceeding three years or to both."

While sections 643(4) and (5) of the UK Companies Act reads:

"(4) If the directors make a solvency statement without having reasonable grounds for the opinions expressed in it, and the statement is delivered to the registrar, an offence is committed by every director who is in default.

(5) A person guilty of an offence under subsection (4) is liable-

(a) on conviction on indictment, to imprisonment for a term not exceeding two years or a fine (or both);

(b) on summary conviction-

(i) in England and Wales, to imprisonment for a term not exceeding twelve months or to a fine not exceeding the statutory maximum (or both);

(ii) in Scotland or Northern Ireland, to imprisonment for a term not exceeding six months, or to a fine not exceeding the statutory maximum (or both)."

5.09 The CLRC also retains the recommendation that in the event a company becomes unable to pay its debts within the period specified in the solvency statement the company should be allowed to recover any sum of money received by the shareholders as a result of the reduction except where they have received the distribution in good faith.

Recommendation 3.11

The CLRC recommends that a provision on arriving at the list of creditors be included as part of the capital reduction provisions.

Recommendation 3.12

The CLRC recommends that creditors be enabled to object to the reduction of capital exercise by the company (whether private or public). The objection may be made within four weeks after the special resolution is passed. The grounds for objection should be specified in the statutory provision and that these are where the creditors have not been offered security for the debts or any other safeguards, or that the company does not have sufficient assets.

Recommendation 3.13

The CLRC recommends that where a creditor objects to a capital reduction exercise but does not have reasonable grounds to object, he should be liable for costs incurred.

Recommendation 3.14

The CLRC recommends that in the event that a company becomes unable to pay its debts within the period specified in the solvency statement, such company should be entitled to recover from its members the amount which they have received as a result of the reduction of capital of the company except where the distribution was received in good faith.

6. REFORMING THE PROVISIONS ON SHARE BUY BACK

6.01 In CD 8, the CLRC recommended some changes to the share buy back provisions. The CLRC recommended that a solvency test, similar to that introduced under the alternative procedure for capital reduction should be adopted for section 67A of the Companies Act 1965. However, under the share buy back provisions, it should not be necessary for all the directors to make a declaration. Instead, the declaration of solvency should be made by a majority of the directors or if there are only two directors, by both of them. There were positive responses to these recommendations and thus the CLRC retains these recommendations.

6.02 The CLRC also recommended that the restriction of having to sell the shares “on the market” should be removed. This will enable the legal framework to be put at par with other jurisdictions such as UK and Singapore and enable companies to have better options on how to deal with the treasury shares. While there are concerns that there could be abuse,³⁵ it is to be noted that a share buy back is mainly undertaken by a public listed company in accordance with the relevant rules of the Stock Exchange. The CLRC is of the view that the safeguards such as those provided for under the Bursa Malaysia Securities Berhad Listing Requirements will be able to minimise the possibility of abuse. The CLRC thus retains the recommendations relating to share buy back in CD 8.

³⁵ One respondent was of the view that the treasury share could be sold to friendly parties for the benefit of the controlling shareholders and that this can be detrimental to the minority shareholders of the company. Another respondent was of the view that by allowing the resale of Treasury shares off market, a change in the control of the company may be effected under circumstances which are less transparent for the market which may lead to abuse and manipulation.

- 6.03 The CLRC has also sought views on whether a time frame should be specified for the treasury shares to be resold failing which the shares are considered as cancelled. However, respondents were of the view that there is no need for such restrictive provision. The current requirement of Bursa Malaysia Securities Berhad already provide that the authority granted by members via an ordinary resolution passed at a general meeting for the company to carry out the share buy back may only continue in force until the conclusion of the next AGM wherein the said authority shall lapse unless it is renewed or until the expiration of the period within which the next AGM is required by law to be held. The CLRC does not recommend the introduction of a time frame within which treasury shares are to be resold and does not recommend that the treasury shares be cancelled if the shares were not resold within the time frame.
- 6.04 The CLRC has also suggested that section 67A(3C) should be redrafted in view of the confusion in relation to the wordings of the section and its impact on substantial shareholding. As noted in CD 8, a share buy back may inadvertently create a substantial shareholder or changes in the shareholding of an existing substantial shareholder through no conduct of the person. The CLRC recommends that section 67A(3C) should clearly state that the company shall have no voting rights or the right to share in any distribution (i.e. dividends or distribution of assets upon a winding up) and that the treasury shares are to be treated as carrying no voting rights but shall continue to be ordinary shares of the company.³⁶

³⁶ This requires the deletion of the wording in section 67A(3C) that states "treasury shares shall not be taken into account in calculating the number or percentage of shares or class of shares in the company for any purposes, including, without limiting the generality of this provision, the provisions of any law or requirements of listing rules of a Stock Exchange on substantial shareholding, takeovers, ..." As a comparison, the Singapore Companies Act provides that the company shall not exercise any right in respect of the treasury shares and this includes any right to attend or vote at meetings. The company shall be treated as having no right to vote and the treasury shares shall be treated as having no voting rights: section 76(2) and (3). In addition, no dividends may be paid and no other distribution in respect of the company's assets, including distribution in a winding-up, may be made to the company in respect of the treasury shares: section 76(4).

Section 726 of the UK Companies Act 2006 states that "The company must not exercise any right in respect of the treasury shares, and any purported exercise of such a right is void. This applies, in particular, to any right to attend or vote at meetings." In addition "No dividend may be paid, and no other distribution (whether in cash or otherwise) of the company's assets (including any distribution of assets to members on a winding-up) may be made to the company, in respect of the treasury shares."

Recommendation 3.14

The CLRC recommends the introduction of a solvency test for a share buy back. The declaration of solvency is to be made by a majority of the directors.

Recommendation 3.15

The CLRC recommends the removal of the words “on the market of the Stock Exchange on which the shares are quoted” in section 67A(3B)(b) of the Companies Act 1965. This will enable treasury shares to be sold not just on the stock exchange but also via direct business transactions.

Recommendation 3.16

The CLRC recommends that section 67A(3C) of the Companies Act 1965 should clearly state that a company shall have no voting rights or the right to share in any distribution (i.e. dividends or distribution of assets upon a winding up) attached to its treasury shares and that the treasury shares are to be treated as carrying no voting rights but shall continue to be ordinary shares of the company.

7. REFORMING SECTION 67 OF THE COMPANIES ACT 1965

7.01 In CD 8, the CLRC recommended that a company should be allowed to give financial assistance for the purpose of or in connection with a purchase of or subscription for its own shares or in the shares of its holding company by a special resolution of the shareholders. The company must also satisfy the solvency test before a company may give any such financial assistance. It is the recommendation of the CLRC that the same solvency test as proposed under the reduction of capital regime be adopted under this provision. However, only a majority of the directors will be required to make the solvency declaration. A majority of the respondents are in agreement with these recommendations.

7.02 In CD 8, the CLRC sought views on whether it should be possible for directors to approve the giving of such financial assistance without having to obtain the approval of shareholders where the amount of the financial assistance inclusive of the amounts of any other financial assistance by the company does not exceed 5% or 10% of the shareholders' fund. The majority of the respondents were of the view that shareholders' approval should still be required. It was felt that should the decision to give financial assistance be left solely to the board, there will be a risk that this may lead to abuse.

Recommendation 3.17

The CLRC recommends that:

- (d) a company be permitted to give financial assistance for the purpose of or in connection with the purchase of or subscription for its shares or shares in its holding company provided the company is able to satisfy the solvency test and provided that a special resolution is passed by its shareholders to authorise the giving of such financial assistance;
- (e) the solvency test proposed for a reduction of capital and share buy back be adopted for such financial assistance;
- (f) the solvency statement be made by a majority of the directors and personal liability be imposed on the directors for making a statement which is not based on reasonable grounds.

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Chapter Four

Corporate Insolvency

CHAPTER FOUR - CORPORATE INSOLVENCY

1. INTRODUCTION

1.01 The main thrust of this chapter is to review and propose a legal and regulatory framework:

- that will enable companies that could not continue its business as a going concern to be wound up in an efficient manner,
- that will enable companies that are facing financial difficulties, but where there is a business case for the continuation for the company's business, to be restructured.

1.02 The liquidation process is discussed in Part A of this chapter. The review relating to the liquidation process is conducted to ensure that the statutory provisions are of continued relevance and are clear so as to enable an efficient liquidation process without further diminishing the company's assets to the detriment of the company's creditors. In Part B of this chapter, the CLRC considered the introduction of a corporate rehabilitation framework to help revitalise ailing companies in Malaysia where there is a business case for the companies to continue their business through a corporate rehabilitation framework, rather than liquidation. An efficient corporate insolvency framework that provides options to businesses to wind up or to be rehabilitated will promote the efficient and sustainable use of economic resources and encourage private sector development and growth. This chapter also discusses improvement to schemes of arrangement, the receivership process and company charges.

PART A - COMPANY LIQUIDATION - REFORMS AND RESTATEMENT OF THE LAW

2. RESTATEMENT OF THE LIQUIDATION PROVISIONS

2.01 In CD 4, the CLRC recommended that section 219(2) of the Companies Act 1965 be amended to provide that in the case of a compulsory winding up, the commencement date of winding up is the date the order to wind up the company is made by the court. However, there were concerns that creditors' interest would be undermined if a compulsory winding up commences from the date the order was made and not the date of the filing of the petition, especially in relation to sections 223, 224, 293, 294 and 295. As noted in CD 4, corollary changes to these sections in relation to the definition of commencement of compulsory winding up must be made to ensure that the amendment to section 219 will not have the unintended consequences of enabling dissipation of a company's assets during the period leading to the winding up. This may be done by de-linking these sections from section 219(2).

Recommendation 4.1

The CLRC recommends that section 219(2) of the Companies Act 1965 be amended to provide that the commencement date of a compulsory winding up is the date the order to wind up the company is made by the court.

A. List of Exempt Dispositions

2.02 The present legal framework states that all dispositions of the company's assets after the presentation of the winding up petition are void, unless these are validated by the court. The practice to obtain a validation order from the court to enable the day-to-

day business of the company to continue is too cumbersome and costly. The company may still need to continue its operations despite the fact that a petition for winding up has been filed against it. In CD 4, the CLRC has recommended that section 223 of the Companies Act 1965 be amended by inserting a list of dispositions which are exempted from the requirement to obtain a validation order from the court. This recommendation received positive responses. The insertion of a list of exempt dispositions will provide certainty and be more cost effective as it will ease the burden faced by companies.

Recommendation 4.2

The CLRC recommends the introduction of a list of exempt dispositions so that transactions which are exempt dispositions do not require any validation order from the court.

3. UNDUE PREFERENCE TRANSACTIONS

3.01 In CD 4, the CLRC reviewed section 293 of the Companies Act 1965 which identifies what are undue preference transactions that may be set aside by the liquidator.³⁷

3.02 There were several issues highlighted in CD 4. One of the shortcomings of section 293 is the fact that section 293 is not clear as to what amounts to undue preference transactions. The objective of the rules regarding undue preference transactions is to prevent one creditor from obtaining an unfair advantage over the other creditors by

³⁷ An undue preference transaction is a transaction that has the effect of giving a creditor a preference over the other creditors where the transaction was entered into by a company when the company was unable to pay its debts or the transaction was entered into within a specific time before the commencement of winding up. For the purpose of section 293 of the Companies Act 1965, the specific time frame is within six months from the date of commencement of winding up. The time frame of six months is not specified in section 293 of the Companies Act 1965, therefore, a cross-reference has to be made to section 53 of the Bankruptcy Act 1967.

concluding a transaction within the twilight period before the commencement of winding up. However, there is uncertainty whether there is a need for a liquidator to prove intention by the company to prefer some creditors over the other creditors under section 293 of the Companies Act 1965.³⁸

3.03 The CLRC has recommended that section 293 of the Companies Act 1965 should be amended by clarifying that there is no necessity to prove an intention to prefer certain creditors and that the transactions should be set aside if the effect of such transaction is to have a preference of one creditor over the other creditors. The recommended section 293 should adopt an “effect-based” test which means a voidable transaction can be set aside based on its effect, regardless of the intention, motive, or knowledge of the debtor or the recipient of the transaction. The CLRC also retains its recommendation in CD 4 to introduce a list of undue preference transactions to be modelled after the New Zealand provision³⁹ but with modifications as to the time frame.⁴⁰

3.04 Another shortcoming of section 293 highlighted by CD 4 is the fact that section 293 requires cross-referencing to section 53 of the Bankruptcy Act 1967 to ascertain the time frame within which a transaction may be considered as an undue preference transaction. In line with the objective to simplify and clarify the law, the CLRC has recommended that the current practice of cross-referencing to the Bankruptcy Act

³⁸ See *Sime Diamond Leasing (M) Sdn Bhd v JB Precision Moulding Industries Sdn Bhd* [1998] 4 MLJ 569.

³⁹ See section 292 of the New Zealand Companies Act 1993.

⁴⁰ Section 292 of the New Zealand Companies Act 1993 has two different time periods:

- transactions occurring within the specified period of two years of formal insolvency
- transactions occurring within the restricted period of six months of the formal insolvency

The two different time frames have been the subject of review by the New Zealand Insolvency Law Review (NZILR) as they were often criticised as being arbitrary and lengthy (see para 2.13 of the CD 4).



1967 be discontinued. This is to be done by incorporating within the Companies Act in relation to the winding up of companies all provisions on undue preference transactions currently under the purview of section 53 of the Bankruptcy Act 1967. The Companies Act will then be the sole legislation for matters concerning companies in liquidation.

- 3.05 In CD 4, the CLRC also recommended retention of the time frame of six months (as currently provided for by section 53 of the Bankruptcy Act 1967) to be the cut-off period to determine whether or not the transaction made become void as an undue preference. In the case of a compulsory winding up, the time frame should be within six months from the date of the presentation of the petition, and where prior to the presentation of the petition, the company passed a resolution to voluntarily wind up the company, the six months period is counted from the time when the resolution was passed. In the case of a voluntary winding up, the time frame should be within six months from the date upon which the voluntary winding up is deemed to have commenced.

Recommendation 4.3

The CLRC recommends removing any cross-referencing to the provisions of the Bankruptcy Act 1967 on issues relating to undue preference transactions under section 293 of the Companies Act 1965 and that all provisions concerning undue preference transactions under the Bankruptcy Act 1967 and any other statutes incorporated into the Companies Act 1965.

Recommendation 4.4

The CLRC recommends the introduction of a list of undue preference transactions by incorporating within the Companies Act 1965 all provisions on undue preference transactions in respect of companies winding up currently under the purview of section 53 of Bankruptcy Act 1967.

4. REVIEW OF SECTION 295 OF THE COMPANIES ACT 1965

4.01 In line with the recommendation to amend provisions relating to the commencement date of winding up, the CLRC recommends that the claw-back provision under section 295 of the Companies Act 1965 be amended to allow a liquidator, in the case of a compulsory winding up, to set aside any voidable transaction if such transaction was entered into within two years from the date of the presentation of the petition or from the date the company passes a resolution to voluntarily wind up the company, whichever is earlier. In the case of a voluntary winding up, the CLRC recommends that the period within which a liquidator may set aside transactions under section 295, is two years from the date upon which the voluntary winding up is deemed by this Act to have commenced.

4.02 In CD 4, the CLRC noted that section 295 may be circumvented by the use of interposed entities. The CLRC recommended that section 295 be amended to extend its application to “persons connected to directors” and to “substantial shareholders of the company”. The respondents to this recommendation agreed that liquidators should have the right to set aside any undervalued transactions entered into by the company with any persons who have connection with the directors of the company or from any substantial shareholders of the company.

Recommendation 4.5

The CLRC recommends that section 295 of the Companies Act 1965 should be extended to “connected persons” which has reference to section 122A of the Companies Act 1965. In relation to a compulsory winding up, the claw-back period should be six months from the date of the presentation of a petition for winding up by the court. For clarity, only the words “commencement of winding up” would be replaced with “the date of presentation of petition for winding up to the court”.

5. INABILITY TO PAY DEBTS AS A GROUND FOR WINDING UP

A. Increasing the Statutory Amount for Demand Notice

5.01 For the purpose of a notice of demand under section 218(2)(a) of the Companies Act 1965, the CLRC has recommended that the threshold of the statutory amount of debt be increased from the present RM500 to RM5,000. A majority of the respondents agreed with the recommendation.

5.02 There are, however, concerns that the threshold amount of RM5,000 may be too high so that it may preclude small creditors from petitioning given the fact that the disparity in income in Malaysia is still too wide. There are also views that the threshold of RM5,000 is still too low and that such threshold should be based on a formula (such as percentage ratios linked to the size of a company).

5.03 Nonetheless, the CLRC agrees to retain its earlier recommendation in CD 4 to increase the threshold on the statutory amount of debts under section 218(2) to RM5,000. A specific figure will also provide certainty. The CLRC felt that the proposed increase is reasonable based on the present economic conditions. The proposed increase will also prevent creditors from abusing section 218 by issuing a statutory demand based on trivial claims against a debtor company with no intention to commence winding up proceedings.

Recommendation 4.6

The CLRC recommends that the threshold of statutory debts under section 218(2) of the Companies Act 1965 be increased to RM5,000.

B. Time Frame for Filing Winding Up Applications

5.04 The CLRC has recommended introducing into section 218(2) of the Companies Act 1965 a time limit within which a petition for winding up must be filed and the proposed time frame should be three months from the expiry of the notice of demand. A time frame would ensure that a debtor company would not be under a constant threat of a winding up petition being presented against it. This will to some extent reduce the possibility of creditors abusing the statutory demand process. However there were concerns that the time frame of three months as earlier suggested may be too short. There were also views that merely fixing the time limit would not alleviate the prospect of abuse of the statutory demand process as creditors would still have the opportunity to issue a fresh demand after the expiry of the time limit and thus leave from the court should also be required before a creditor can be allowed to issue a fresh statutory demand notice. However, the CLRC does not recommend the requirement to obtain leave of court to issue a statutory demand afresh.

Recommendation 4.7

The CLRC recommends that the time frame within which a petition for winding up must be filed should be six months from the expiry of the notice of demand. However, no leave of court should be required to issue a statutory demand afresh.

6. TERMINATION OF WINDING UP PROCEEDINGS

6.01 In CD 4, the CLRC proposed to introduce into the Companies Act a provision for termination of winding up proceedings. A liquidator or a director or a shareholder of a company should be allowed to apply to terminate the winding up proceedings. This will remove the uncertainty as to whether the courts do have the power to terminate winding up proceedings or a winding up order since the current law only authorise a “stay” of the winding up order. There is also a suggestion that section 239 of the Companies Act 1965 should be amended to provide that upon termination of the winding up proceedings, a liquidator may, under section 239 apply for his release and the provision of section 240(4) of the Companies Act 1965 which states “an order of the court releasing the liquidator shall discharge him free from all liability in respect of any act done or default made by him in the administration of the affairs of the company ...” should apply.

Recommendation 4.8

The CLRC recommends:

- (a) that the court be given the power to terminate winding up proceedings on the application of a relevant party; and
- (b) that an application to terminate winding up proceedings may be made by a liquidator, or a director or shareholder of the company or any other entitled person or a creditor of the company, or the Registrar.

7. INTERIM LIQUIDATOR AND LIQUIDATOR

7.01 In CD 4, the CLRC proposed to substitute the current phrase “an approved liquidator provisionally appointed”⁴¹ with the term “interim liquidator”, similar to the New Zealand provision, to ensure clarity in the law. There are views that there is no real confusion in the usage of the term “an approved liquidator provisionally appointed” as there is no distinction with regard to the powers and the purpose for the appointment of a provisional liquidator and a private liquidator. However, the term “provisional liquidator” is used in section 231 to refer to the Official Receiver (OR) or an approved liquidator who is appointed after the presentation of the winding up petition and before the making of the winding up order. The term “provisional liquidator” is also used in section 227(1) of the Companies Act 1965 to refer to the OR who can be a provisional liquidator after the winding up order if an approved liquidator other than the OR is not appointed to be the liquidator of the company. The CLRC, is of the view that section 231 can be clarified by stating that “the court may appoint the Official Receiver or an approved liquidator as interim liquidator at any time after the presentation of a winding up petition and before the making of a winding up order ...”.

Recommendation 4.9

The CLRC recommends that section 231 of the Companies Act 1965 be clarified by stating that “the court may appoint the Official Receiver or an approved liquidator as interim liquidator at any time after the presentation of a winding up petition and before the making of a winding up order ...”.

⁴¹ See section 231 of the Companies Act 1965.



A. Powers of Liquidator

- 7.02 In general, the CLRC has recommended the adoption of the provisions set out under the UK Insolvency Act 1986 in relation to the powers of a liquidator in different types of winding up, with some modifications.
- 7.03 One issue is that the Companies Act 1965 currently requires prior approval from the court or the Committee of Inspection (COI) before an advocate could be appointed to assist a liquidator in a liquidation process. To further facilitate the smooth process of liquidation, the CLRC has recommended abolition of the requirement of the prior approval of the court or the COI before an advocate could be appointed. The CLRC is also of the view that the current requirement to first obtain a sanction from the court or the COI before a liquidator could exercise his power to compromise a debt due to company if the amount of debt is more than RM1,500 is too cumbersome and has caused delay in the liquidation process.
- 7.04 The Companies Act 1965 currently provides that the time frame for the liquidator to trade after the winding up order has been made is up to a period of four weeks. This is too short a period for liquidators to complete the necessary investigations and to decide on the viability of the company to carry on its business. It is more practical to extend this to six months. As noted in CD 4, section 238(2) of the Companies Act 1965 the liquidator is liable to some sanctions if he retains for more than 10 days a sum exceeding two hundred ringgit or any such sum that the court authorizes him to retain unless he explains the retention to the satisfaction of the court. The CLRC is of the view that this sub-section burdensome as section 238(1) is sufficient to cater for the requirement for a liquidator to keep whatever monies he received in a specific bank account. Currently, the company secretaries are under a statutory duty to submit the statement of affairs of the company to the OR within 14 days from the date the

winding up order was made. In CD 4, the CLRC recommended the amendment of section 234 of the Companies Act by deleting the requirement for the company secretaries to submit the statement of affairs. This recommendation is retained. The CLRC is also of the view that while the list of contributories should be prepared by the liquidator, this is useful when there is surplus capital to be distributed. Thus the current mandatory requirement to settle a list of contributories should be amended to make it discretionary for the liquidator to settle the list of contributories if there should be surplus capital for distribution or if there should be contributories that are likely to contribute their unpaid portion of capital.

Recommendation 4.10

The CLRC recommends as follows:

- (a) that the prior approval of the court or the Committee Of Inspection be not required before an advocate could be appointed.
- (b) that a liquidator be empowered to compromise debts owed to the company if the amount is less than RM10,000 and this power should be exercisable without the having to obtain the sanction of the court.
- (c) that the court or the Committee Of Inspection be given a discretionary power to give a blanket approval to liquidators to compromise debts which are above the threshold of RM10,000 but not more than RM50,000 and this power should be exercised on a case to a case basis.
- (d) that the existing time frame for a liquidator to trade after the winding up order has been made be extended to six months, after which the liquidator be required to obtain the sanction of the court.
- (e) that section 238(2) of the Companies Act 1965 be deleted.
- (f) that section 234 of the Companies Act 1965 be amended by deleting the requirement for company secretaries to submit statements of affairs.

- (g) that the current mandatory requirement to settle a list of contributories be amended to make it discretionary for the liquidator to settle the list of contributories if there should be surplus capital for distribution or if there should be contributories who are likely to contribute their unpaid portion of capital.

8. RIGHTS OF SECURED CREDITORS

- 8.01 In CD 4, the CLRC recommended codification of the rights of secured creditors in the Companies Act 1965 along the lines of section 305 of the New Zealand Companies Act 1993. This will clarify the position of secured creditors in respect of the charged asset in the case of liquidation. The CLRC agrees to retain the recommendation. In this respect, corollary changes will have to be made to rule 67 of the Companies (Winding Up) Rules 1972.

Recommendation 4.11

The CLRC recommends the codification of the rights of secured creditors in the Companies Act 1965 along the lines of section 305 of the New Zealand Companies Act 1993.

9. PROOF OF DEBTS UNDER SECTION 291 OF THE COMPANIES ACT 1965

- 9.01 A majority of the respondents agreed with the recommendation to delete any cross reference to the Bankruptcy Act 1967 in relation to proving of debts by creditors under section 291 of the Companies Act 1965. Such an amendment will alleviate the difficulty of cross-referencing to statutes outside the Companies Act.

9.02 The CLRC agrees to retain this recommendation. The CLRC has agreed to incorporate into the Companies Act 1965 all the provisions relating to the proof of debts and the rank of claims by creditors as currently stated in the Bankruptcy Act 1967. This recommendation is consistent with the earlier recommendations in relation to section 293.

Recommendation 4.12

The CLRC recommends that the provisions in relation to proof of debts be retained and that all the provisions relating to the proof of debts and the rank of claims by creditors as currently stated in the Bankruptcy Act 1967 be incorporated into the Companies Act 1965.

10. RIGHT OF SET-OFF

10.01 The CLRC also recommended in CD 4 that the right of set-off by creditors should be codified in the Companies Act 1965. The CLRC also proposed that the right of set-off should not apply to creditors who have reasons to believe that the company is unable to pay its debts.

10.02 However, there are concerns that this exception is not clear. There were also views that the UK provision that the right of set-off does not exist "if the creditor has notice at the time the sums owed became due that a meeting of creditors has been summoned or a petition for the winding up of the company was pending" is clearer. Therefore, the CLRC revises its earlier recommendation and agrees to adopt the UK provision.

Recommendation 4.13

The CLRC recommends that the right of set-off should not be applicable to creditors "if the creditor has notice at the time the sums owed became due that a meeting of creditors has been summoned or a petition for the winding up of the company was pending".

11. PREFERENTIAL DEBTS UNDER SECTION 292 OF THE COMPANIES ACT 1965

11.01 In relation to preferential creditors under section 292 of the Companies Act 1965, the CLRC recommended in CD 4 the retention of section 292 to ensure the protection of certain categories of unsecured creditors in a company under liquidation.

Recommendation 4.14

The CLRC recommends retaining section 292 of the Companies Act 1965.

A. Increasing the Quantum of Wages and Salary

11.02 The CLRC recommended increasing the quantum for wages and salary of employees entitled to priority in a winding up from the present RM1,500 to RM15,000. The recommendation is timely as other jurisdictions such as Singapore, Australia, UK, Hong Kong and New Zealand have amended their provisions to increase such quantum over the years. Furthermore, as pointed out by one respondent, "the value of Ringgit since 1965 (the year in which our Companies Act was introduced) has decreased". The increase is expected to enhance the social obligation of companies towards the well being of their employees. The CLRC feels that the proposed quantum is not only reasonable but fairer to employees, especially those in the lower income category who will be affected the most in the event the company goes into liquidation.

Recommendation 4.15

The CLRC recommends increasing the quantum for wages and salary of employees entitled to priority in the winding up of a company from the present RM1,500 to RM15,000.

B. New Definition of “Wages and Salary of Employees”

11.03 The CLRC proposed the introduction of a new definition of “wages and salary of employees” which shall include payment in lieu of notice of termination of employment and payment of gratuity for termination of employment by reason of winding up.

11.04 This proposal received mixed reactions from the respondents, especially the recommendation to include payment of gratuity in the definition of “wages and salary of employees”. There are views that the inclusion of “payment in lieu of notice of termination of employment” and “payment of gratuity” should be viewed as incentives to providing a better scheme of protection for employees of a company. There are, however, views that a mandatory obligation to pay gratuity to employees in the event the company goes into liquidation should not be imposed on the company as payment of gratuity should always be voluntary in nature. In practice, it always derives from the contract of employment between the employees and the company. If the contract of employment is silent on this issue no gratuity should be paid out. However, there is nothing to stop the company from giving some form of gratuity to its employees if the company is willing to do so and if there are sufficient assets for distribution.

Recommendation 4.16

The CLRC recommends excluding “payment of gratuity for termination of employment” from the definition of “wages and salary of employees” in section 292 of the Companies Act 1965.

C. Federal Taxes

11.05 At present, federal taxes are given preferential treatment under section 292(1)(f) of the Companies Act 1965. The CLRC has proposed to abolish any preference given to the government in respect of any unpaid taxes of a company under liquidation. The government has other means to enforce the collection of taxes from companies including the right to make the directors of companies personally liable and to establish a more stringent process in the collection of tax. However, employees and small unsecured creditors do not have available to them the same resources as the government has. Therefore, a better scheme of preferred debts is the only solution for them in enforcing their right of recovery in the event of liquidation.

Recommendation 4.17

The CLRC recommends abolishing any preference given in the winding up of a company to the government in respect of any unpaid taxes of a company under liquidation.

12. PROCESS OF STRIKING NAME OFF THE REGISTER

12.01 The CLRC recommended in CD 4 that a liquidator should be allowed to apply to the Registrar to strike off a wound up company under section 308(3) of the Companies Act 1965. This will facilitate the process of dissolution of a company in a more orderly manner as all the company's affairs have been fully wound up and the company is no longer in operation. Opinions, however, differ in the case of dormant companies under section 308(1). There are views that directors should also be given the mandate to make such an application, subject to approval by the members. In the case where the directors and shareholders are not contactable, the company secretary should be allowed to make the application.

12.02 SSM has introduced new guidelines on applications to strike off the name of a company under section 308 with effect from 12 January 2007. The issuance of the new guidelines is intended to cater for applications requesting the Registrar to invoke his power under section 308(1) and (3) of the Companies Act 1965. Under the new guidelines, directors and shareholders of a defunct company are allowed to make an application to strike off the name of the company under section 308(1) whilst a liquidator may do so under section 308(3) subject to the fulfilment of requirements in the guidelines. SSM also made a stand that company secretaries are not the appropriate party that should be allowed to make the application as they are not the owners of the company. The new guidelines are in line with the recommendations made by the CLRC.

PART B: A CORPORATE REHABILITATION FRAMEWORK

13. INTRODUCTION

13.01 The CLRC recommends that the proposed corporate rehabilitation framework should have the following key features:

- (a) a clear framework for rehabilitation that is easily understood and implemented;
- (b) a realistic time frame within which the proposal is to be prepared, approved and implemented;
- (c) a moratorium period to enable the proposal to be formulated and implemented without the threat of liquidation or creditors' action that may frustrate the rehabilitation process;
- (d) provisions to safeguard creditors' interest by adequately providing for creditors' voting rights and the right to receive reliable information concerning the company and the rehabilitation plan;
- (e) the involvement of qualified insolvency practitioners to ensure that the process would be impartial and there would be no unnecessary delay in the process; and
- (f) the court's involvement in the initiation, implementation and supervision of the rehabilitation plan to ensure fairness in the process and to ensure that the rights of any particular class are not prejudiced.

13.02 In CD 10, the CLRC recommended the introduction of new corporate rehabilitation schemes in the forms of a Judicial Management System and a Corporate Voluntary Arrangement (CVA). The new schemes will complement the existing provisions for a scheme of arrangement under section 176 of the Companies Act 1965 which enables a financially distressed company to restructure where there is a business case

for it to continue its operations. In making the following recommendations, the CLRC referred to corresponding legislation in UK, Singapore and Australia.

14. JUDICIAL MANAGEMENT

14.01 A judicial management scheme is initiated by an application made by a company or a company's creditors to place the management of a company in the hands of a qualified insolvency practitioner with the necessary skill and experience to be known as a Judicial Manager. The Judicial Manager, once appointed by the court, will prepare a restructuring plan which must be acceptable to the majority of the creditors. Once approved by the creditors and sanctioned by the court, the plan will be implemented.

Recommendation 4.18

The CLRC recommends that the court should be empowered to make a judicial management order in relation to a company if it is satisfied that the company is or will be unable to pay its debts and it considers that the making of the order would be likely to:

- (a) achieve the company's survival on the whole or in part ; and
- (b) enable a more advantageous realisation of the company's assets than in a winding up.

For this purpose, a company "will be unable to pay its debts" if any of the circumstances as stated in section 218(2) of the Companies Act 1965 should arise.

Recommendation 4.19

The CLRC recommends that parties who may be entitled to apply for a judicial management order be the company or its directors (pursuant to an ordinary resolution of its members or a resolution of the board of directors) or a creditor or creditors of the company (including prospective and contingent creditors). However, the court should not make the order if:

- (a) a receiver and manager has been or will be appointed or the making of the order is opposed by a person who is entitled to appoint a receiver and manager, e.g. a debenture holder; or
- (b) the company is in liquidation or the company is a bank or a finance company or an insurance company licensed under the relevant Act.

14.02 The CLRC noted that there was a suggestion that notice of the application for a judicial management order should be given to a company's debenture holders prior to the application being made. The CLRC recommends that when an application for a judicial management order is made to the court, notice shall be given to the company, in a case where a creditor is the applicant, and to any person who has appointed or is or may be entitled to appoint a receiver and manager of the whole (or substantially the whole) of a company's property under the terms of any debentures of the company. This would enable the relevant parties to be informed of the application and where appropriate, to oppose the making of the judicial management order.

Recommendation 4.20

The CLRC recommends that when an application for a judicial management order is made to the court, notice of the application should to be served on:

- (a) the company with respect to which the order is sought to be made, in a case where a creditor is the applicant; and
- (b) any person who has appointed or is or may be entitled to appoint a receiver and manager of the whole (or substantially the whole) of such company's property under the terms of any debenture of such company.

A. Moratorium Period

14.03 A moratorium is an important feature of a judicial management scheme and enables the judicial manager to prepare the rehabilitation plan without any potential threat of a winding up of the company or any court action by the creditors which may likely frustrate the judicial management process.

Recommendation 4.21

The CLRC recommends that once a petition for a judicial management order has been made, an interim judicial manager may be appointed by the court, although this should not be required in all situations. The CLRC further recommends that during the period beginning with the making of an application for a judicial management order and ending with the making of such an order or the dismissal of the application:

- (a) no resolution should be passed or order made for the winding up of the company;
- (b) no steps should be taken to enforce any charge or security over the company's assets without leave of the court; and
- (c) no proceedings against the company should be commenced or continued without leave of the court.

Recommendation 4.22

The CLRC recommends that at the hearing of an application for a judicial management order, the court should be entitled to exercise its discretion in deciding whether or not to make a judicial management order. Once a judicial management order is made, a moratorium should be in place during which:

- (a) no winding up order can be made against the company and any petition for winding up shall be dismissed;
- (b) any receiver and manager appointed shall vacate office and no new appointment of any receiver and manager shall be permitted;
- (c) no enforcement of any charge or security or repossession of hire purchase goods shall be permitted;
- (d) no other legal proceedings against the company shall be commenced or continued except with leave of the court.

14.04 The CLRC also recommended that any transfer of shares or any alteration in the status of members of a company with respect to which a judicial management order has been made during the moratorium period shall also be void unless the court otherwise orders. While there was support for this, there were concerns about how this will affect listed companies whose shares are traded on an almost daily basis.

Recommendation 4.23

The CLRC recommends that with the exception of companies listed on the Bursa Malaysia Securities Berhad any transfer of shares or any alteration in the status of members of a company with respect to which a judicial management order has been made during the moratorium period shall be void unless the court otherwise orders.

14.05 In CD 10, the CLRC recommended that the judicial manager be given 180 days to table a proposal, and where appropriate the court may give an extension of time to the judicial manager to do so. While respondents agree that the judicial manager be given 180 days and an extension of time, where appropriate, to table the proposal and obtain the creditors' approval, there are views that there should not be granted an unlimited number of extensions. This is because of concerns that the moratorium period may be abused by the company to prevent creditors from enforcing their contractual and security rights against the company. As such, a maximum moratorium period of one year is proposed. The CLRC felt that the period is sufficient for the judicial manager to come up with a viable plan and to implement it. The period of moratorium plays a crucial role in enabling a judicial manager to draw up a workable rehabilitation proposal to the satisfaction of all parties concerned.

Recommendation 4.24

The CLRC recommends that the judicial manager should be given 180 days to table a proposal to creditors, and where appropriate the court should be entitled to give an extension of time to the judicial manager to do so, but the maximum duration of the moratorium should be one year after the order appointing the judicial manager is made.

Recommendation 4.25

The CLRC recommends that the moratorium which takes effect upon the appointment of a judicial manager should be effective for 180 days from the date the order is made unless earlier discharged or further extended by the court.

14.06 There are also suggestions that:

- (a) utility suppliers with monopolistic control such as Tenaga Nasional Berhad (TNB), Telekom, etc. should be obliged to continue to provide supplies to a company with respect to which a judicial management order has been made so long as the new debts incurred are paid. They should not cease supply or discontinue services on the ground that the "old debts" are not paid;
- (b) no steps are to be taken to commence or to continue the enforcement of a sale of land of such a company under the National Land Code except with the leave of the court.

Recommendation 4.26

The CLRC recommends that:

- (a) utility suppliers with monopolistic control such as Tenaga Nasional Berhad (TNB), Telekom, etc. should be obliged to continue to provide supplies to a company with respect to which a judicial management order has been made so long as new debts incurred by such a company are paid;
- (b) no steps be permitted to be taken to commence or to continue the enforcement of a sale of land of such a company under the National Land Code except with the leave of the court.

14.07 There were also concerns that the moratorium does not expressly deal with the effect of the Limitation Act and that it is not clear whether the limitation period is suspended during the moratorium.

Recommendation 4.27

The CLRC recommends that a statutory provision be enacted stating that the limitation period shall not run with respect to any cause of action against a company in relation to which a judicial management order has been made during the moratorium period and that the moratorium period should be excluded for the purpose of calculating the limitation period.

B. Creditors' Rights And Voting By Creditors

14.08 In CD 10, the CLRC recommended that the judicial manager should be given 180 days to prepare the rehabilitation plan and have the proposal tabled to creditors at the creditors' meeting for their approval. The CLRC also recommended that the proposal must be approved by a majority in value of the creditors who are present and voting at the meeting. Only creditors who have had their proof accepted by the judicial manager may be allowed to vote. However, the majority of the respondents were of the view that a higher majority of creditors should be required to approve the proposal.

14.09 In CD 10, the CLRC expressed the view that to ensure that the judicial manager achieves the objectives of the judicial management, the creditors should be allowed to modify the proposal subject to approval by the judicial manager. However, some respondents were concerned that any modification may cause delays in the implementation of the proposal as not all creditors have the same interests, which could lead to multiple proposals for modifications. There were also concerns that allowing for modification during the voting stage could adversely affect the interest of the creditors who are not present or that the persons representing the creditors may not have the mandate to approve the modified proposal. The CLRC believes

that some flexibility should be given to the judicial manager to deal with concerns of the creditors, and so long as the judicial manager is able to obtain the creditors' approval within the stipulated statutory duration (i.e. 180 days which may be extended to not more than one year after the order is made), and notice of any prior changes to the proposal are given to creditors to be voted upon, modifications to the proposal should not be prohibited. Ideally, when the proposal is tabled before creditors, the creditors should either vote for or against the proposal. If the proposal is voted against, the creditors should vote for the modified proposal in the next meeting. It is up to the judicial manager to take into account the request for modification during or after the creditors' meeting since the judicial manager will have to consent to the modified proposal.

- 14.10 An important issue raised in CD 10 relates to whether a proposal that has been agreed to may be defeated by any other creditors. While the law in UK allows secured creditors to elect not to be bound by the judicial management or administration, this has been identified as one of the deficiencies of the regime. In Australia, a secured creditor holding a charge over the whole or substantially the whole of the company's assets may effectively veto the administration after the order is made. However, the court may restrict these rights. As stated in CD 10, the practice in Australia is to obtain the cooperation of a chargee who holds an all embracing charge and often there will be a discussion before the voluntary administration begins; there is evidence that the secured creditors often do not utilise this remedy. As stated in CD 10, the CLRC is of the view that the Singapore approach is more suitable to Malaysia where once the judicial management order has been made and the proposal tabled has been approved by the creditors' meetings, all creditors are bound by the proposal. A secured creditor who wishes not to be bound by the judicial management order must take the initiative to oppose the petition. However, once the judicial management order has been made all creditors shall be bound. This will ensure that the rehabilitation plan can be implemented especially if it involves

disposal of any of the company's assets. On this point, the judicial manager should also be given the power to deal with the charged property of the company as if the property were not subject to the security.

14.11 Reporting obligations should also be imposed on the judicial manager. As stated in CD 10, the judicial manager should be required to report the result of the creditors' meeting to the court and the Registrar.

14.12 The CLRC is also of the view that creditors' right would be better protected if they are given the right to bring an action for oppression if they have grounds to prove that the affairs of the company during the judicial management process has been conducted in an oppressive manner.

Recommendation 4.28

The CLRC recommends that at a creditors' meeting convened to consider a proposal tabled by the judicial manager, not less than a 75% majority in value of creditors, present and voting either in person or by proxy, whose claims have been accepted by the judicial manager, be the requisite majority to approve the proposal with modifications, subject to the judicial manager's consent to each modification.

Recommendation 4.29

The CLRC recommends that any secured creditor be given the right to oppose the petition or application for a judicial management order. However, once the judicial management order has been made the secured creditors should not be permitted to realize their security and the judicial manager should have the power to deal with the charged property of the company as if the property were not subject to the security. There should also be an express statutory provision that once the proposal is approved, it shall be binding on all creditors of the company whether or not they have voted in favour of the proposal.

Recommendation 4.30

The CLRC recommends that the judicial manager should be required to report the results of the creditors' meeting to the court and to notify the Registrar of the same. In addition, the decision of the creditors' meeting should be advertised in the national daily newspapers, at least one in English and one in Bahasa Malaysia.

Recommendation 4.31

The CLRC recommends that creditors should be able to bring an action for relief against oppressive conduct if the court is satisfied the company's affairs, property or business are being or have been managed by the judicial manager in a manner which is or was unfairly prejudicial to the interests of its creditors or members generally or of some part of its creditors or members.

C. Ending the Judicial Management

14.12 The CLRC recommends that the judicial management order should be capable of being discharged prior to the expiry of the period referred to in the following sentence. The judicial manager should have has a 180 days period or if extended by the court, a maximum period of one year to obtain creditors' approval for the proposal.

14.13 In CD 10, the CLRC recommended that there should be three situations under which a judicial management order may be discharged. The CLRC retains its recommendation that the judicial management order should be discharged in the following situations:

- (a) if the proposal has not been approved by the requisite majority in the creditors' meeting and where the court orders the discharge of the judicial manager. If a report is given to the court that the meeting has declined to approve the judicial manager's proposals (with or without modifications), the court should be entitled by order to discharge the judicial management order and make such consequential provision as it thinks fit, or adjourn the hearing conditionally or unconditionally, or make an interim order or any other order that it thinks fit;
- (b) if the purpose of the judicial management has been successfully achieved;
- (c) if the judicial manager is of the view that the purpose of judicial management is unachievable. In this situation, the judicial manager shall apply to the court for the judicial management order to be discharged.

There were also views from respondents that if the judicial manager applies for a discharge, or is no longer qualified to be a judicial manager or is removed from office, the court may appoint a replacement instead of ending the judicial management scheme.

Recommendation 4.32

The CLRC recommends that the judicial management order should be discharged in the following situations:

- (a) if the proposal has not been approved by the requisite majority in the creditors' meeting and where the court orders the discharge of the judicial manager. The court should be entitled by order to discharge the judicial management order and make such consequential provision as it thinks fit, or adjourn the hearing conditionally or unconditionally, or make an interim order or any other order that it thinks fit;
- (b) if the purpose of the judicial management has been successfully achieved;
- (c) if the judicial manager is of the view that the purpose of judicial management is unachievable;
- (d) if the judicial manager applies for a discharge, or is no longer qualified to be a

judicial manager or is removed from office, unless the court makes an order replacing the existing judicial manager.

D. The Role and Functions of the Judicial Manager

14.14 The recommendation to adopt the powers of the judicial manager as stipulated under section 227G of the Singapore Companies Act (Chapter 50) was favoured by most of the respondents. It is necessary to expressly specify the powers of a judicial manager in the statute to clarify the extent of powers of the judicial manager. The powers should be included in a separate schedule similar to the corresponding provisions found in the UK Insolvency Act 1986.

Recommendation 4.33

The CLRC recommends that the powers of the judicial manager should be expressly provided for in the companies legislation and the adoption of the powers of the judicial manager as stipulated under section 227G of the Singapore Companies Act (Chapter 50).

E. Judicial Manager as an Agent of the Company

14.15 To enable the judicial manager to act on behalf of the company, the CLRC recommended that the judicial manager should be deemed to be the agent of the company. This recognition allows the judicial manager to have control over the affairs, business and property of the company during the period of judicial management thus enabling him to implement the scheme without any interference from the management of the company. The respondents unanimously agreed with this recommendation.

Recommendation 4.34

The CLRC recommends that the judicial manager should be deemed to be the agent of the company during the period of judicial management.

Recommendation 4.35

The CLRC recommends that the judicial manager should be given control over the affairs, business and property of the company during the judicial management period.

14.16 To ensure the objectives of the rehabilitation plan are achieved, the judicial manager should be allowed to implement the proposal effectively. In this respect, the CLRC recommended that the powers of the other officers of the company be suspended unless the judicial manager gives his approval in writing. This provision is to ensure that there will be no interference from the management of the company. The respondents concurred with this recommendation unanimously. In addition, it was suggested that the power and responsibility to ensure that statutory obligations are complied with, for example, lodgement of documents with SSM and convening the AGM, should remain with the officers of the company.

Recommendation 4.36

The CLRC recommends the suspension of powers of the other officers of the company during the judicial management period unless written approval is obtained from the judicial manager.

14.17 The CLRC also consulted on whether the company secretary should be excluded from the duty to submit the statement of affairs. However, the majority view is that while a company secretary as an officer of the company should not be the sole person to be responsible for the submission of the statement of affairs, he should not be exempted from liability. Other officers such as directors and other key management of the company should also share this responsibility.

Recommendation 4.37

The CLRC recommends that a company secretary should not be exempted from the duty to submit the statement of affairs to the judicial manager.

F. Personal Liability in Contracts

14.18 In CD 10, the CLRC recommended that a judicial manager should be allowed to exclude personal liability in any contract entered into by him or adopted by him so that he is personally liable unless he disclaims such liability. Some of the respondents indicated that a judicial manager should only be excluded from liability for past contracts and that he should be personally liable for contracts he enters into during the judicial management process, similar to the Singapore position. A strong view was expressed that it would be too onerous to impose upon a judicial manager personal liability for contracts which he enters into for and on behalf of a company under judicial management as he does not benefit from such contracts. As such he should not be expected to be responsible for bona fide commercial obligations if he is acting in the interest of the company.

Recommendation 4.38

The CLRC recommends that a judicial manager should be allowed to exclude personal liability in any contract entered into by him or adopted by him so that he is personally liable unless he disclaims such liability.

G. Indemnity

14.19 Although a judicial manager should be permitted to exclude personal liability for contracts, the CLRC further recommended that he should be indemnified in respect of his liabilities, remuneration and expenses, out of the assets of the company in priority to all other debts except those subject to security of a non-floating nature. This would be in line with the priority given to a claim by a liquidator under section 292(1) of the Companies Act 1965 and the proposed recommendation in respect of a receiver's remuneration found in paragraph 5.6 of CD 10. Another view is that claims under the indemnity should take priority over all other debts of the company including those subject to both fixed and floating charge.

Recommendation 4.39

The CLRC recommends that a judicial manager should be indemnified in respect of his liabilities, remuneration and expenses, out of the assets of the company in priority to all other debts except those subject to security of a non-floating nature.

15. CORPORATE VOLUNTARY ARRANGEMENT (CVA)

15.01 The recommendation to introduce a CVA regime modelled after the UK CVA received overwhelming support from the respondents. A financially distressed company may now opt to initiate a rehabilitation scheme by itself through the appointment of a qualified insolvency practitioner who will supervise the implementation of this scheme.

Recommendation 4.40

The CLRC recommends the introduction of a statutory Corporate Voluntary Arrangement scheme along the lines of that provided under the laws of the UK, with modifications, if necessary.

A. Moratorium Applies to both Small and Large Companies

15.02 Unlike the UK approach which limits the moratorium to small companies only, the proposed CVA for Malaysia intends to enable both small and large companies to apply for a moratorium of the relevant proceedings. This is to enable the implementation of the scheme so that the scheme is not impeded by any actions taken by creditors of the company.

Recommendation 4.41

The CLRC recommends that the moratorium period should apply to both small and large companies seeking to propose a Corporate Voluntary Arrangement scheme in its rehabilitation process.

15.03 The moratorium period in a CVA automatically commences from the filing of relevant documents in court. There is no requirement to apply for a court order. This recommendation is supported by the majority of the respondents. This is in line with the objective of the CVA that is to rehabilitate the business of an ailing company as a going concern in a speedier and quicker manner with minimal court intervention.

Recommendation 4.42

The CLRC recommends that a moratorium period for a Corporate Voluntary Arrangement scheme should be automatically in force upon the filing of relevant documents in court without the need for a court order.

15.04 In CD 10, the CLRC recommended following the UK CVA by allowing a 28-day moratorium period to get the proposal approved. If the period is not sufficient, extension is to be allowed with the leave from the court. However such an extension must have a definite end date to prevent the CVA from being abused. Thus, the CLRC recommends that a moratorium could only be extended for up to 60 days if both the creditors and the insolvency practitioner agree to it.

Recommendation 4.43

The CLRC recommends that a moratorium period for a Corporate Voluntary Arrangement scheme may be extended for up to 60 days if both the creditors and the insolvency practitioner agree to it.

15.05 The CLRC has recommended that the court's involvement should be limited to hearing challenges on the grounds of material irregularity, unfair prejudice to the interest of a creditor or member, or that the CVA is anticipated to be ineffective in practice.

Recommendation 4.44

The CLRC recommends that the court's involvement in a Corporate Voluntary Arrangement should be limited to hearing challenges to such scheme on the grounds of material irregularity, or unfair prejudice to the interest of a creditor or member or that such scheme is anticipated to be ineffective in practice.

Recommendation 4.45

The CLRC recommends that the proposal for a Corporate Voluntary Arrangement scheme be approved by a majority vote of not less than 75% of the total value of the creditors who may vote in person or by proxy and that the proposal as so approved would be binding on the creditors of the company and that any modifications to the proposal should not be allowed. If there were any modifications, the creditors should vote on any modified proposal in the next meeting. The result of the meeting should also be reported to the court.

Recommendation 4.46

The CLRC recommends that Corporate Voluntary Arrangement scheme itself or the procedure involved in its approval should be subject to challenge in court. An application for such challenge should be made within 28 days beginning with the first day the report is made to the court. If a creditor alleges that he has not been given notice, he should be entitled to challenge the decision of the meeting within 28 days of the day on which he became aware that the meeting had taken place.

Recommendation 4.47

The CLRC recommends that the management of a financially distressed company under a Corporate Voluntary Arrangement scheme should remain with the directors.

16. SCHEME OF ARRANGEMENT (SECTION 176)

16.01 While the CLRC has recommended alternatives to the corporate rehabilitation framework in the forms of the Judicial Management System and the CVA, the CLRC is of the view that section 176 is still relevant. Section 176 is required if there is to be a rearrangement of the rights of members and creditors and when it was necessary to compromise creditors' claims against an insolvent company. Nonetheless, since the CLRC is introducing the judicial management and CVA schemes, there may be less

need to rely on section 176 when the company is insolvent. However, the CLRC is of the view that section 176 should still be retained to provide another option for the kind of compromises that can be made with members and creditors of a company.

16.02 The CLRC noted that the present section 176 has been used as a delaying mechanism by companies to frustrate the enforcement of any judgment debts by their creditors. One of the modifications recommended by the CLRC in CD 10 is to retain the post-1998 amendments with the emphasis that the period of the moratorium should be limited to one year only. The CLRC further recommended that extension to the moratorium period should be allowed and such extensions shall be subject to a maximum period of one year only. There should not be any further extension after the period of one year even if the company fails to come up with a viable reorganisation plan. After the period of moratorium has ended, the creditors are free to take whatever necessary actions to enforce their claims against the company. This is to prevent abuse by companies who only apply for the restraining order without having in place a viable and workable restructuring plan.

16.03 The CLRC has also recommended the appointment of a qualified insolvency practitioner to assess the viability of the scheme. In a financially distressed company, the opinion of a third party who is an expert in that field should be mandatory to ensure that the reorganisation scheme takes into account the interest of all stakeholders.

16.04 The CLRC further recommends that the corporate and securities market regulators should not be prevented from commencing any enforcement actions to ensure compliance of corporate and/or securities law or guidelines thereunder. There should be the introduction of a general exception provision containing circumstances in which regulators may be allowed to exercise powers despite the moratorium.

Recommendation 4.48

The CLRC recommends that if the 90-day period of the moratorium for a scheme of arrangement between a company and its creditors is extended, it should be limited to not more than one year.

Recommendation 4.49

The CLRC recommends the appointment of a qualified insolvency practitioner to assess the viability of a scheme of arrangement between a company and its creditors.

Recommendation 4.50

The CLRC recommends that the moratorium for a scheme of arrangement between a company and its creditors should not be effective against the companies and securities market regulators so as to prevent them from commencing any enforcement actions to ensure compliance of corporate and/or securities law or guidelines thereunder.

PART C: REVIEWING THE COMPANY RECEIVERSHIP PROCESS

17. CODIFICATION OF THE AGENCY STATUS OF A RECEIVER

17.01 In CD 10, the CLRC discussed whether the agency status of a receiver should be codified. The CLRC is of the view that codification will resolve the ambiguity in relation to the receiver's status where the agency status of a receiver is not provided in or has been inadvertently left out from the debenture. The CLRC recommends that the agency status of a receiver be codified in the Companies Act.

17.02 It should also be stated that the receiver becomes the agent of the company upon his appointment by the debenture holder notwithstanding the commencement of winding up. Where a liquidator has been appointed, the consent of the liquidator or the court in case of consent being withheld by the liquidator should be obtained before the receiver may continue to be the agent of the company. In such situations, the liquidator should not unreasonably withhold his consent. If the liquidator refuses consent, he should state the reason for his refusal. This recommendation received favourable support from the respondents as it encourages the efficiency of the receivership process when the company is in liquidation because the receiver is able to continue to carry on business as agent of the company.

Recommendation 4.51

The CLRC recommends that:

- (a) the agency status of the receiver or a receiver and manager be codified;
- (b) once a company is in liquidation and a liquidator has been appointed, a receiver should be empowered to continue to act as the agent of the company to carry on the business of the company, provided he obtains consent from the liquidator which

must not be unreasonably withheld, or if the liquidator withholds his consent, the consent of the court;

- (c) the agency status of the receiver or receiver and manager over the assets secured under the debenture should continue after the appointment of the liquidator.

18. POWERS OF A RECEIVER

18.01 In CD 10, the CLRC recommended that the powers of a receiver be codified under statute. There should be a codification of a minimum list of powers which should be applicable as a default provision in case the debenture is silent as to the powers of a receiver. These powers may be expressly modified or excluded by the debenture. Where the debenture is silent, the codified powers shall prevail. This adds clarity on which powers (statute or those found in the debenture) prevail.

Recommendation 4.52

The CLRC recommends that there should be a codification of a minimum list of powers which should be applicable as a default provision in case the debenture is silent as to the powers of a receiver.

19. LIABILITY OF A RECEIVER AND INDEMNITY

19.01 The CLRC has recommended that the receiver is to be personally liable for debts incurred by him or his authorised agent during his tenure unless there is a specific agreement to the contrary between the contracting parties. If the receiver is not personally liable for the contracts he enters into during his tenure, this will deter third parties from dealing with the receiver. Many respondents suggest that the receiver should be personally liable for the contracts entered into by him unless he contracts out of personal liability.

Recommendation 4.53

The CLRC recommends that a receiver should be personally liable for debts incurred by him or his authorised agents during his tenure of office, unless there is a specific agreement to the contrary between the contracting parties.

- 19.2 Although a receiver is to be personally liable for contracts he enters into unless stated otherwise in the contract, he has the right to be indemnified out of the assets of the company. The indemnity shall be paid in priority to any charge or other security held by any debenture holder. This recommendation is fully supported by the respondents.

Recommendation 4.54

The CLRC recommends that a receiver should have the right to be indemnified out of the assets of the company which are charged under the debenture pursuant to which the receiver is appointed.

20. RECEIVER'S COSTS TO BE GIVEN PREFERENTIAL TREATMENT

- 20.01 The CLRC is of the view that the receiver's costs and remuneration should be paid in priority over claims by any other creditors, and that the costs and expenses of winding up and receivership should be given priority as preferential debts that will be paid first out of the assets subject to a floating charge. Priority claims over assets of the company in insolvency should also be consolidated under the provisions of the Companies Act 1965 and should take precedence over provisions of any other Acts of Parliament. This position will clarify the ambiguity in the event of dispute and conflict.

Recommendation 4.55

The CLRC recommends that the receiver's cost and remuneration should be given priority over all claims by other creditors.

PART D: COMPANY CHARGES AND REGISTRATION PROCESS

21. IMPROVEMENTS TO THE PRESENT REGISTRATION SYSTEM

21.01 The registration regime for company charges is intended to provide information to third parties as to encumbrances over a company's assets and is useful to enable third parties to decide whether or not to provide credit to a company. While registration of company charges is necessary, in CD 10, the CLRC discussed the viability of changing the current charges registration system, specifically the introduction of a notice-filing system. However, as stated in CD 10, the CLRC noted that any introduction of a new system such as a notice-filing system would be difficult to implement if issues pertaining to automated filing (e.g. e-filing) and reconciliation of document flow and the coordination in the registration process of a company's charged asset with the various authorities (e.g. land office, patent office) are not resolved.

21.02 In addition, in a notice-filing system, there is a possibility that the charge may not be created subsequent to the advance filing of the notice, and thus additional rules may need to be put in place to deal with these notices, creating complexity in the registration process. The present registration system is based on the fact that a charge has been created and is registered after creation. A notice-filing system means that the charge need not be created before it is registered. The Steering Committee of the UK CLR considered this issue and stated that this may be dealt with by either requiring confirmation of a notice filed in advance or providing for its cancellation. However, the CLRC is of the view that this will add on to the costs of business and may cause confusion especially if there is accidental omission in either confirming the notice filing or cancelling the notice filing. Furthermore, the CLRC is also of the view that the issue of priority may be resolved by providing that the charge, if registered,

is to be effective from the date of registration as is the case under the Australian Corporations Act 2001.⁴²

Recommendation 4.56

The CLRC recommends that:

- (a) the requirement that a charge which is required to be registered under the Companies Act 1965 be registered within 30 days of the date of its creation be retained, and
- (b) a charge be given priority from the date of its creation once it has been registered with the Registrar.

21.03 In CD 10, the CLRC recommended the deletion of section 108(9) to avoid confusion with regard to the requirement of registration of charges under the Companies Act 1965 and registration of assets under other specialised registries which serves different purposes. All the respondents unanimously agreed with the recommendation.

Recommendation 4.57

The CLRC recommends deletion of section 108(9) of the Companies Act 1965.

21.04 As the requirement to register a charge under the Companies Act 1965 has a different purpose from that of registration in other specialist registers, the CLRC recommends that the existing practice on dual registration should be maintained.

Recommendation 4.58

The CLRC recommends retaining the provision on dual registration of charges.

⁴² Section 261(2) and (3) of the Corporations Act 2001 states that when a charge is so registered, it has the priority accorded to a registered charge from the time of its registration and such registration does not prejudice any priority that would have been accorded to the charge under any other law (whether an Australian law or not) if the charge had not been registered.



21.05 The CLRC recommended the modification of Form 34 to include the words “the interested party”. Many agreed, provided that the interested party is a licensed financial institution under the BAFIA to prevent abuse by any person claiming to be a chargee. The proposed modification will be in line with the wording stated in section 109(1) that the documents may be lodged for registration by “the company concerned or by any other person interested in the documents”.

Recommendation 4.59

The CLRC recommends modifying Form 34 to include the words “the interested party”.

22. LIST OF REGISTRABLE CHARGES

22.01 In CD 10, the CLRC expressed the view that a revision of the list of registrable charges must bear in mind the following:

- (a) the charge must be over a company's asset; and
- (b) the list of registrable charges must be general enough to cover new types of asset.

As stated in CD 10, there is less compliance cost for companies in retaining the present position. The risk of listing the types of registrable charges is that it may cause problems when new types of assets are created and the list is construed as exhaustive. Those who support the view of having a list of registrable and non-registrable charges stated that having two lists (for registrable and non-registrable charges) will minimise confusion as to the types of charges that require registration. The lists would have to be drafted in broad terms to cover any new securities in the future. With this approach, the lists would not be exhaustive in their application. The CLRC is of the view that an important consideration is whether the list of registrable charges is sufficiently clear and is couched in sufficiently wide terms so as to cover any new types of securities over a company's assets.

Recommendation 4.60

The CLRC recommends the retention of the current system for the registration of charges but acknowledges that having a list of registrable and non-registrable charges is another option and the risk of the list being construed as exhaustive can be mitigated against with proper drafting of the section.

Chapter Five

Review of Criminal, Civil and Administrative Sanctions in the Companies Act 1965

CHAPTER FIVE

REVIEW OF CRIMINAL, CIVIL AND ADMINISTRATIVE SANCTIONS IN THE COMPANIES ACT 1965

1. INTRODUCTION - GENERAL PRICIPLES FOR REVIEW

1.01 In CD 11, the CLRC considered the various enforcement tools that are generally available to the regulator in enforcing compliance with the Companies Act 1965, or to the company and/or shareholders of their rights under the Companies Act 1965 or the common law. The CLRC reiterates its views in CD 11 that:

- (a) The sanctions regime under the Companies Act 1965 should be one that deters undesirable conduct and practices but at the same time promotes responsible risk taking. This requires a sanctions regime that takes into consideration the types of sanctions that may be imposed and the appropriateness of such sanctions in relation to the contravention.
- (b) The sanctions regime should comprise a range of enforcement tools ranging from administrative sanctions and civil remedies to the more severe criminal sanctions or disqualification order or winding up.

2. THE USE OF CRIMINAL SANCTIONS

2.01 The CLRC reiterates its views in CD 11 that criminal sanctions should be reserved for the most serious cases of contravention or non-compliance, particularly involving fraud or deliberate wrongdoing or dishonesty. In CD 11, the CLRC also identified examples of such wrongdoings, i.e. section 304 (the fraudulent trading provision), section 368 (fraud by officers) and sections 364 and 364A (the offence of making false or misleading statements or reports) of the Companies Act 1965.

A. Duties of Directors

2.02 The CLRC recommends that the statutory provisions on directors' duties should be enforced by a range of sanctions where the regulator should be authorised to bring criminal proceedings and/or civil proceedings. Criminal sanctions for the contravention of directors' duties should be imposed where the contravention is accompanied by fraud or dishonesty. Where there is no fraud or dishonesty, the contravention should not be criminalised. Instead, the regulator should be authorised to initiate civil penalty proceedings. At the same time, private redress for breach of directors' duties should still be available to the company or its members.

Recommendation 5.1

The CLRC recommends that the regulator should be authorised to bring either criminal or civil proceedings for any contravention of the statutory provisions on directors' duties.

Recommendation 5.2

The CLRC recommends that criminal liability for the contravention of directors' duties should be imposed where the contravention is accompanied by fraud or dishonesty. Where there is no such fraud or dishonesty, the contravention should not be criminalised but the regulator should be empowered to bring civil proceedings.

B. Offences Arising from Non-compliance with Disclosure/Procedural requirements

2.03 The majority of the offences in the Companies Act 1965 are related to non-compliance with disclosure/procedural requirements. The CLRC is of the view that criminal sanctions should still be generally used to ensure compliance with the obligation to disclose. However, not all failures to comply with procedural requirements should give rise to criminal sanctions.

Recommendation 5.3

The CLRC recommends that there should be criminal liability imposed for non-compliance with disclosure obligations. Where the non-compliance relates to other procedural requirements, such failures should not give rise to criminal liability.

C. On whom should criminal sanctions be imposed?

2.04 An effective sanctions regime in relation to the Companies Act 1965 should consider whether the sanction is imposed on the appropriate person, i.e. whether the sanction is imposed on the company and/or the officer in default.

Recommendation 5.4

The CLRC recommends that in cases where a contravention involves fraud or deliberate wrongdoing or dishonesty, criminal liability should be imposed on officers involved in the contravention and not the company.

Recommendation 5.5

The CLRC recommends that the general penalty provision under section 369 of the Companies Act 1965 should be revised to reflect the view that whether or not there should be criminal liability for a contravention of any section of the Companies Act 1965 should be decided on a "section by section" basis.

Recommendation 5.6

The CLRC recommends that in the case of non-compliance with procedural requirements, criminal liability on the company should be removed where there are meaningful and alternative sanctions available which can be imposed on individuals who are involved in the contravention.

Recommendation 5.7

The CLRC recommends that the definition of “officer in default” should be revised to state as follows:

“An officer is ‘in default’ for the purposes of the provision if he authorises or permits or participates in the contravention.”

3. CIVIL ACTIONS BY THE REGULATOR

3.01 In CD 11, the CLRC sought views as to whether the regulator should be authorised to commence civil penalty proceedings for breach of directors' duties. The CLRC reiterates its views in CD 11 that the regulator should be empowered to initiate civil proceedings if it appears to the regulator, i.e. SSM, that it is in the interest of the public for a company to sue a director to recover compensation from the director who has breached his duty. The amount of compensation recovered should first be utilised to reimburse the regulator for all costs incurred in respect of investigations or proceedings in relation to the contravention and second, to compensate aggrieved persons who have suffered losses or damage as a result of the contravention.⁴³ Nonetheless, the current private enforcement regime that enables members or the company to initiate a civil action where there is contravention of corporate law should be retained.

⁴³ See sections 200 and 358 of the Capital Market and Services Act 2007.



3.02 The majority of the respondents support this view but there were concerns as to whether criminal and civil proceedings may be commenced concurrently and whether civil proceedings by the company and/or shareholders will be allowed to be initiated when the regulator has initiated civil proceeding. The CLRC is of the view that a criminal action should be allowed to be commenced against a director even though civil proceedings are underway or have been resolved. In addition, civil proceedings by the company and/or shareholders should still be allowed even though the regulator has initiated civil proceedings.

Recommendation 5.8

The CLRC recommends that the regulator should be given a general power to initiate civil proceedings on behalf of the company if it appears that it is in the interest of the public to do so. The amount of compensation recovered should first be utilised to reimburse the regulator for all costs incurred in respect of investigations or proceedings in relation to the contravention and second, to compensate aggrieved persons who have suffered loss or damage as a result of the contravention. A criminal action against a director should be permitted even though civil proceedings are underway or have been resolved. In addition, civil proceedings by the company and/or shareholders should be permitted even though the regulator has initiated civil proceedings.

4. THE USE OF ADMINISTRATIVE SANCTIONS

4.01 The Companies Act 1965 also contains provisions for administrative sanctions that may be utilised by the regulator. These administrative sanctions enable the regulator to effectively and efficiently use regulatory resources.

Recommendation 5.9

The CLRC recommends that administrative sanctions in the Companies Act 1965 should be retained but that their use should be best applied for small and relatively insignificant regulatory contraventions.

5. CIVIL REGULATORY SANCTIONS - DIRECTORS' DISQUALIFICATION PROVISIONS

5.01 The CLRC is of the view that the disqualification provisions as well as the regulator's authority to commence the winding up of a company should be retained. However, the current disqualification provisions in the Companies Act 1965 should be modified as stated below.

Recommendation 5.10

The CLRC recommends that section 130 of the Companies Act 1965 should be retained but clarified to state that a person who is disqualified under the section ceases to hold office as a director of a corporation and ceases to be entitled to be directly or indirectly concerned or to take part in the management in Malaysia of a corporation for so long as he shall be disqualified.

Recommendation 5.11

The CLRC recommends that the current position in relation to automatic disqualification should be retained, i.e. that there should be automatic disqualification for:

- (a) conviction of an offence involving fraud or dishonesty;
- (b) being an undischarged bankrupt;
- (c) conviction in relation to offences in connection with the promotion, formation or management of a company, or under section 132 or 303 of the Companies Act 1965.

Recommendation 5.12

The CLRC recommends that a director who has contravened the legislative provisions relating to directors' duties may be disqualified upon an application by the regulator.

Recommendation 5.13

The CLRC recommends that the Companies Act 1965 should enable a disqualification order to be made if there is persistent default or contravention of the Act.

Recommendation 5.14

The CLRC recommends that section 130A of the Companies Act 1965 should be clarified to state that a person may be disqualified if within the last five years, the person has been a director of two or more companies when they were wound up in insolvency and that the manner in which the companies were managed, including the director's conduct in relation to the management, business or property of the companies, was wholly or partially responsible for the companies' insolvent liquidation.

Recommendation 5.15

The CLRC recommends that there should be publicity of the persons against whom a disqualification order has been made.

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Advocate & Solicitor
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6. Y. A. Tuan Abdul Alim Abdullah (5 January 2004 - 31 August 2005)
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Representative from the Prime Minister's Department
21. En. Mat Ghani bin Abdullah (26 November 2004 - 15 August 2006)
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Representative of the Insolvency Department
24. Puan Rohatul Akmar Abdullah (5 January 2004 - 13 July 2004)
Representative from the Prime Minister's Department
25. En. Jeswant Singh (5 January 2004 - 13 July 2004)
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4. Puan Norhaiza Jemon
5. Puan Sapiah Ambo
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LIST OF RESPONDENTS

1. General Insurance Association of Malaysia (PIAM)
2. Institute of Approved Company Secretaries (IACS)
3. Malaysian Accounting Standards Board (MASB)
4. Malaysian Institute of Accountants (MIA)
5. Malaysian Association of Company Secretaries (MACS)
6. The Malaysian Institute of Chartered Secretaries and Administrators (MAICSA)
7. Association of Merchant Banks in Malaysia (AMBM)
8. The Association of Banks in Malaysia (ABM)
9. Securities Commission (SC)
10. Bank Negara Malaysia (BNM)
11. Mohd Noh & Co.
12. Khazanah Nasional
13. Johor Bahru (JB) Practitioners Group
14. Puan Judy Lim on behalf of Protem Committee of Buyers of Coral Vista Condominium, Subang Jaya
15. Symphony House
16. PFA Corporate Services Sdn Bhd
17. Sunway Management Sdn Bhd
18. Persatuan Firma-Firma Akauntan Awam Melayu Malaysia
19. Wong Beh & Toh
20. Tahan Insurance
21. Shearn Delamore & Co.

22. Joint MIA-MICPA Working Group on Corporate Law Reform
23. The Association of Chartered Certified Accountants (ACCA)
24. Shook Lin & Bok
25. Hong Leong Group Malaysia
26. Employees Provident Fund (EPF)
27. CPA Australia
28. Company Secretary, Telekom Malaysia Berhad.
29. Malaysian Association of Asset Managers (MAAM)
30. Malaysian Investment Banking Association (MIBA)
31. Bar Council Malaysia
32. En. Lim Peng Hock
33. PFA Corporate Services Sdn Bhd
34. Lee Hishammuddin Allen & Gledhill
35. En. Chan Hua Eng
36. Minority Shareholder Watchdog Group (MSWG)
37. The Malaysian Institute of Certified Public Accountants (CPA)
38. Joint MIA-MICPA Working Group on Law Reform
39. Tay & Partners
40. Maybank
41. Kadir, Andri & partners
42. Dr. Mohammad Rizal Salim

43. En. Lam Kee Soon
44. En. Nik Mohd Hasyudeen Yusoff
45. K H Goh & Co
46. En. Billy Kang
47. En. Ang Chen Tong
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49. Takaful Malaysia
50. AMCAF
51. PFA
52. Dr. S. Susela Devi
53. Toh See Hong (Confidentiality Requested)
54. Unit Perancang Ekonomi (EPU)
55. Suruhanjaya Sekuriti
56. Malaysian Employers Federation (MEF)
57. Shearn Delamore & Co
58. Great Eastern
59. Ernst & Young
60. Group A

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