



Legal Herald

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Message from the Managing Partner

My appointment as managing partner on 1 March this year could not have come at a more challenging time. The financial crisis had already made its presence felt in Malaysia and law firms everywhere outside Malaysia were freezing salaries, if not laying off partners and associates.

Fortunately, our firm had already put its plans in motion in early 2008, and our goals remain unchanged – to provide the best quality of work and service to our clients with the best lawyers and staff to make that delivery. We have been cautious with our budgets, but I am happy to say that we have not had to impose a reduction in partners, associates or staff.

Instead, we have been listening to our clients and friends as well as to our own people. And we have formulated strategies to fill in the gaps which we have identified, and I am pleased to report that these are being implemented with the same intensity of purpose as in the making of them.

This bumper issue of our *Legal Herald* underlines our effort to improve the quality of our brand – and I am happy to say that future issues will maintain the variety of input from our teams of partners and associates which will reflect the depth and variety of legal talent in our firm.

To supplement our quarterly publications of the *Legal Herald*, and with a view to

keeping our clients and friends up to date with changes in legal developments, the firm recently launched an electronic copy of our Legal Updates, which is released monthly by email. Any “hotter” news will be issued directly from our practice groups as e-Alerts. Feedback on our publications is always welcome.

With a view to enhancing the quality of our lawyers, we have established a formal programme of in-house training focused on improving the needs of our practice groups and our clients. We look to enhancing the knowledge and practice management skills of our lawyers to set them apart from the rest.

These are just some of the initiatives we have undertaken to improve our quality of work and service to our clients.

I have not had the opportunity to meet all our clients. Certainly that remains my objective. I am thankful to those who have taken the time to share their expectations with us. There is no better feedback than directly from our own clients and friends, especially when they value us enough to be candid.

On behalf of everyone at the firm, I wish to thank all our clients and friends for continuing to allow us the privilege of being of service, and we look forward to riding out these challenging times with you.

With best wishes,
Muthanna

Private Finance Initiatives in Malaysia

by Suleen Ding and Tay Weng Hwee

Governments have, and more so in current times of “financial crisis”, been looking at more efficient ways of implementing infrastructure and services traditionally financed by public funds. In this regard, the United Kingdom took the lead by introducing, over a decade ago, an alternative mechanism commonly known as the “private finance initiative” (“PFI”), which has since been adopted with success in Australia, Hong Kong and other developed countries.

Malaysia appears now to be actively encouraging PFIs and it will be interesting to see its development in this country.

What is a PFI?

The key characteristic of a PFI is the transfer of both funding and construction risks to the private sector. There is no funding from the government at the beginning of the project. Instead, a concession is granted and the private sector contractors fund the project themselves, either through equity or third party financing, or a combination of both.

Upon completion of the project, the contractor does not step out of the picture but continues to operate and maintain the facilities and recovers the project costs from the government in the form of lease charges. These lease charges are measured against the levels, quality and timeliness of the service provided throughout the duration of the concession. When the concession period expires, the assets and facilities are either transferred to the public sector or remain with the contractor.

In many ways, PFIs remind us of the build-operate-own (“BOO”) and build-operate-transfer (“BOT”) projects that have been common in Asia. The difference between the two is the method in which the proposed projects are evaluated.

Proposals under PFIs are assessed to see if it is more cost effective for the private sector to undertake the project compared to the public sector. Hong Kong, for instance, evaluates PFI proposals against a “public sector comparator”, which is the cost to the government of delivering the project itself.

Malaysia has also recognised this method of assessment and, in the Ninth Malaysia Plan, mentions the public sector comparator.¹

Projects suitable for PFI

As the costs to the public and private sectors in procuring services through PFIs can be substantial, PFIs are usually more suitable for bigger projects that can justify such costs. Traditionally, PFIs are used in projects where:

- the investments are sizeable;
- the performance of the contractor is easily measured;
- the relevant assets are specific; and
- there are no significant concerns with regard to the involvement of the private sector in such projects.

Projects that have been popular with PFIs include those involving the construction of roads, railways and airport terminals.

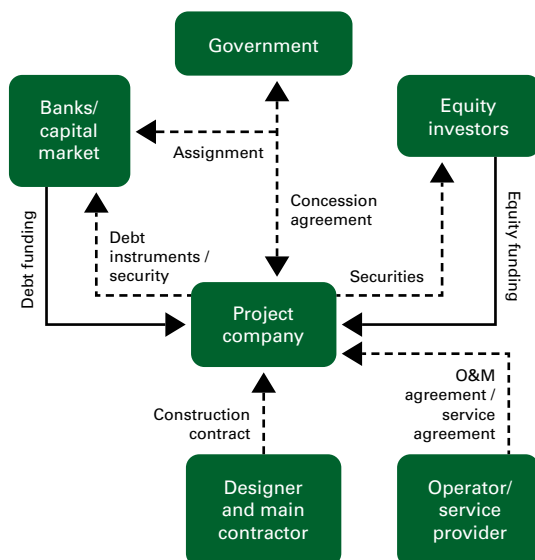
¹ See www.epu.gov.my/rm9/english/Chapter10.pdf, paragraph 10.23 at p 230

More recently, PFIs have been used for the building of schools, universities, hospitals and social housing, which have conventionally been seen as projects best carried out by the public sector. Given the obvious interest of the public in such projects, the rationale for allowing the private sector to undertake such projects is that as long as proper documents are in place, the risks are appropriately allocated and there is strict supervision, there is no real reason why the private sector, if it can do a better job, should not be involved in such projects.

Further, the manner in which PFIs are typically structured is seen as safeguarding the proper allocation of risks, strict supervision and documentation of the obligations of the parties involved.

Structure of a PFI

Although each project is unique, the following structure would be typical for a PFI:



Documentation in a PFI can be quite extensive. The contracts between the various parties as illustrated in the diagram will include:

- a concession or project agreement under which the project company in the private sector is appointed by the government to undertake the design and construction of the infrastructure and operation and maintenance of the facilities throughout the duration of the concession;
- a shareholders’ agreement between equity investors to regulate their rights in respect of the project company;
- debt instruments or a facilities agreement and related security documents in respect of the financing granted to the project company for the project;
- a construction contract between the project company and the main contractor (which usually contains terms that mirror those in the concession agreement); and
- an operation and maintenance or service agreement between the project company and the operator or service provider (which, similarly, contains terms that mirror those in the concession agreement).

PFIs in Malaysia

(a) *The Ninth Malaysia Plan*

In a clear move towards usage of PFIs, the Ninth Malaysia Plan or 9MP envisages the implementation of PFI projects from year 2006 to 2010. Some policies and requirements surrounding PFIs spelt out in the 9MP include:

- Thirty percent of the equity of privatised entities shall be allocated to bumiputera entrepreneurs.

- At least 60% of contract works shall be awarded to bumiputera participants.
- Participants must have access to capital, including having a minimum paid-up capital of RM250,000 when proposing a project, and access to additional financial support within a year of signing the concession agreement.
- Participants must have technical and management expertise.
- The selection of concessionaires will be done through a bidding process.
- A public sector comparator will be established to evaluate whether the private sector can carry out the projects at a more competitive price. The government will invoke a value-for-money test and projects will only be awarded to the private sector if the cost of doing so is lower than the public sector comparator's benchmark.
- Lease payments will be tied to a reward and penalty system, whereby profit margins are attractive when key performance indicators are met while deductions will be imposed when service levels are unfulfilled.

Following the launch of the 9MP by former prime minister Tun Abdullah Ahmad Badawi on 31 March 2006, the ministry of finance set up a special purpose vehicle called PFI Sdn Bhd. It is tasked with overseeing and undertaking the implementation of RM20 billion worth of PFI projects allocated under the 9MP involving the education, housing, healthcare and transport sectors.

However, the government has yet to publish a proper framework and a set of guidelines for the implementation of PFI projects in Malaysia along the lines of what has been done by the United Kingdom and other countries.

(b) *Second stimulus package*

In the wake of the current global economic crisis, the government on 10 March 2009 announced a second stimulus package of RM60 billion, of which RM2 billion have been allocated to assist the implementation of PFI projects.

In tabling the second stimulus package in Parliament recently, new prime minister Datuk Seri Najib Tun Razak outlined the following criteria for a PFI:

- The private sector will implement, finance and assume project risks. Project revenue must be generated mainly from the private sector, and not from government sources.
- Government financial help will only constitute a small proportion of the project investment cost. The assistance will act as a tipping point, enabling a marginally non-viable project to become viable.
- Projects must be in strategic sectors such as education and health and tourism, have high spillover effects, create sustainable job opportunities and enhance the nation's competitiveness.²

² See [www.mit.org.my/PDF/Mini%20Budget%20Speech%20-%20Supplementary%20Supply%20\(2009\)%20Bill%202009.pdf](http://www.mit.org.my/PDF/Mini%20Budget%20Speech%20-%20Supplementary%20Supply%20(2009)%20Bill%202009.pdf), at p 24

Under these criteria, it would appear that the government's PFI projects will be limited to those that are relatively self-sufficient, i.e. projects that are commercially viable and revenue generating. This is a deviation from traditional PFIs, which have effectively consisted of projects involving public infrastructure or services that are not ordinarily self-sufficient (e.g. government schools or hospitals).

It is unlikely, however, that PFIs will be confined strictly to a particular class of project. This is apparent from the PFI projects that have been approved as PFIs – the provision of infrastructure for the Tanjung Agas industrial park in Johor, a biotechnology cluster at Iskandar Malaysia, as well as upgrades of the traffic infrastructure system around KL Sentral.³

(c) *Liberalisation of the services sector*

In an attempt to stimulate greater inflow of investments into the country, the government on 22 April 2009 liberalised 27 services sub-sectors by removing the existing equity conditions.⁴ These sub-sectors include health and social services and transport services, which are areas for which PFI projects have been allocated under the 9MP. It would appear, therefore, that the stipulation on 30% bumiputera equity imposed in the 9MP is no longer required of project companies embarking on PFI projects in these sectors, at least until further notice.

As for the other sectors, we have yet to see how restricting the pool of potential participants will affect the efficiency for which PFI is the mechanism of choice.

Conclusions

The experience in other countries has been that PFIs can facilitate a right mix of the private sector in public sector works. For the private sector, PFIs provide opportunities to pursue potentially profitable contracts with the government while for the public sector, PFIs are useful when budgets are tight or need to be controlled.

With the right implementation and commitment of both the public and the private sectors, PFIs as a mechanism have been successful in the delivery of projects.

In line with the government's plan to increase the usage of PFIs in Malaysia, one would expect the issuance by the government of a proper framework and a set of guidelines for the implementation of PFI projects in the near future.

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³ Ibid, page 25

⁴ See www.pmo.gov.my/?menu=news&page=1729&news_id=39&news_cat=4

Case Commentary

McDonald's v McCurry: Which Way Will the Pendulum Swing in the Law of Passing Off?

by Bahari Yeow

In 2001, US-based McDonald's Corporation ("McDonald's") initiated a claim in Malaysia against McCurry Restaurant (KL) Sdn Bhd ("McCurry") for passing off, both of the traditional and "extended" kind, in relation to the latter's use of the trade name "McCurry" (see box on page 8, "Traditional and 'extended' passing off").

After a five-year battle, the High Court ruled in McDonald's favour. McCurry then appealed the decision. In April 2009, the Court of Appeal allowed the appeal, thus overturning the High Court's decision.

Brief facts

McDonald's is the proprietor of a chain of fast-food restaurants in over 100 countries, and opened its first outlet in Malaysia in 1982. McCurry, a Malaysian company that changed its name from Penang Curry House (KL) Sdn Bhd to its present name in 1998, runs a food outlet offering Indian and other Malaysian food.

McDonald's has registered its trade mark having the prefix "Mc" in several countries, including Malaysia. It considers the prefix "Mc" as its trade mark and its source and trade identifier. In the course of its trade, McDonald's has used the distinctive "Mc" for its range of products, such as "McChicken", "McMuffin", "McRendang", "McValue Meal" and "McNuggets".

It argued that the use of "Mc" with "Curry" was deceptive and that, therefore, McCurry was misrepresenting itself as being associated with McDonald's. McCurry's defence was that its menu, which comprised items such as fish head curry, chicken tandoori, naan and tosai, was distinguishable from McDonald's and that the

latter could not have a monopoly over the prefix because "Mc" has been in use for centuries, by the Scottish, for example.

McDonald's relied on the tort of passing off as its cause of action. The issue before the High Court was whether McCurry, by adopting "Mc" for its own restaurant, could be held liable under passing off, both in the traditional and "extended" form.

Elements of tort

Briefly, a plaintiff in an action based on the law of passing off must prove three elements:

- (1) there must be goodwill attached to the plaintiff's mark;
- (2) there must have been a misrepresentation by the defendant leading to confusion or deception; and
- (3) the plaintiff has suffered or is likely to suffer damage as a result of the misrepresentation.

See *Seet Chuan Seng v Tee Yih Jia Food Manufacturing Pte Ltd* [1994] 3 CLJ 7 (SC); *SV Beverages Holdings Sdn Bhd v Kickapoo (Malaysia) Sdn Bhd* [2008] 4 CLJ 20 (CA) and *Sinma Medical Products (M) Sdn Bhd v Yomeishu Seizo Co Ltd* [2004] 3 CLJ 815 (CA).

The High Court decision

The High Court was of the view that McDonald's had proven its case both on the traditional and "extended" forms of passing off. For the "extended" form, the High Court held that McCurry had unlawfully appropriated McDonald's trade mark, thereby resulting in loss and damage.

The Court of Appeal decision

The Court of Appeal, however, held that the use of the word “McCurry” did not amount to a passing off of McDonald’s trade name for the following reasons:

McDonald’s	McCurry
1. The get-up consists of a distinctive golden arched “M” with the word “McDonald’s” against a red background	The signboard has the words “Restoran McCurry” with the lettering in white and grey on a red background, with a picture of a chicken giving a double thumbs up and the wording, “Malaysian Chicken Curry”
2. The food items all carry the prefix “Mc”	None of the food items carry the prefix “Mc”
3. Serves cheeseburgers, French fries and shakes	Sole outlet caters only typically Indian food and local dishes
4. Customers are mainly children	Customers are mainly adults and senior citizens

On the ‘extended’ tort

Gopal Sri Ram JCA (now FCJ) was of the view that:

“... **the common law is not static. It does not rest upon a Procrustean bed. It is organic. And flexible.** It grows to meet changing conditions with dynamism. So, as the nature of trade and commerce developed, so did the tort. As persons found new ways committing ‘theft’ of intellectual property, the common law rose to the challenge.” (emphasis added)

His Lordship further held:

“I am therefore inclined to agree with the submission of counsel for the plaintiff that **the so-called extended tort is nothing more than the common law adapting the tort of passing off to new and different circumstances.**” (emphasis added)

On the UK *McIndian* case

The High Court had relied on *Matter of Application no. 1412458*, in which the trade mark office in the UK denied registration of the mark “McIndian” on the ground that it could be confusingly similar to McDonald’s prefix “Mc”.

The Court of Appeal found that the trial judge had failed to distinguish the facts of *McIndian*. *McIndian* not only sold Indian food but also Southern fried chicken, cheeseburgers, French fries and shakes – the very items sold at McDonald’s. The Court of Appeal held that this constituted a serious misdirection that resulted in a miscarriage of justice.

The Singapore *Future Enterprises* cases

The Court of Appeal relied on the decision in *McDonald’s Corp v Future Enterprises Pte Ltd* [2005] 1 SLR 177, in which Future Enterprises sought to register three application marks, all with an eagle device. The Singapore Court of Appeal held that the presence of the eagle device in “MacTea”, “MacChocolate” and “MacNoodles” made the marks more distinct from McDonald’s “Mc”.

However, the Court of Appeal did not refer to a subsequent Singapore Court of Appeal decision on a case involving a similar battle between McDonald's and Future Enterprises, in *Future Enterprises Pte Ltd v McDonald's Corp* [2007] 2 SLR 845. Future Enterprises had attempted to register "MacCoffee" as a word mark in Singapore. The Registrar allowed McDonald's opposition to the registration. Both the Singapore High Court and the Court of Appeal dismissed appeals by Future Enterprises.

Effect of the Court of Appeal decision

With the Court of Appeal's decision, McDonald's has lost its exclusivity to its prefix "Mc" in Malaysia – at least until such time as the Federal Court finally resolves the dispute, particularly as to whether the principle of "extended tort" should be accepted into our law of passing off to meet new challenges. And, if such "extended tort" is to apply in Malaysia, to what extent it will free itself from inflexibility.

While the Court of Appeal appeared to be receptive to the concept of "extended passing off", it is unclear as to what conditions need to be fulfilled if an action based on the so-called extended tort is to succeed.

What to expect from the Federal Court

It will be a valuable addition to Malaysian case law in this area if the Federal Court could provide guidance on:

- (1) Whether the "extended tort" is recognised in our law of passing off; and
- (2) If so, to what extent the elements constituting the extended tort would differ from the traditional tort.

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Traditional and 'extended' passing off

Traditional passing off

In an action based on passing off, the claimant must prove goodwill, misrepresentation leading to confusion and deception, and resulting damage.

Extended passing off

The English courts have recognised that passing off can be extended to meet the realities of trade as it evolves over time.

Unfair trading is recognised as a wrong actionable at the suit of other traders who suffer loss of business or goodwill.

The English court has shown itself willing to accept that passing off can be accepted without the need to prove confusion.

About the author

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Carbon Emission Reduction Initiatives in Malaysia

by Ooi Bee Hong

The global climate is changing at an alarming rate. One of the factors – some say the top cause behind this phenomenon – is human activity, and it is unlikely we will be able to ascertain the extent of the impact of human activity on the environment.

The temperature increase observed since the middle of the 20th century has been attributed to increasing greenhouse gas concentrations resulting from human activity such as fossil fuel burning and deforestation. It is said that natural phenomena such as solar variation and volcanoes produced most of the warming from pre-industrial times to 1950, followed by a small cooling effect afterward. These findings have been endorsed by scientific societies and academies of science, several among them the national academies of science of major industrialised countries.¹

Malaysia has been blessed with both conventional and non-conventional sources of energy. As the conventional energy sources – namely oil, gas and coal – being fossil fuels will inevitably deplete, their usage has to be carefully managed. Non-conventional energy resources such as biomass, biogas, municipal waste, solar and mini hydro have been identified as potential sources of fuel for electricity generation.

The Eighth Malaysia Plan

Accordingly, during the Eighth Malaysia Plan (“the 8MP”), renewable energy was included as the fifth fuel in addition to oil, gas, coal and hydro. Other efforts to promote the use of renewable energy included the establishment of the renewable energy database at the Malaysia Energy Centre, or Pusat Tenaga Malaysia.

On the academic front, Universiti Sains Malaysia established the Centre for Education, Training and Research in Renewable Energy and Energy Efficiency (CETREEE) to increase public awareness of the positive attributes of renewable energy and energy efficiency measures.

During the 8MP period, energy efficiency measures were undertaken to moderate the increasing energy intensity trend and to avoid wasteful energy usage. These measures included energy audits in selected industries and in commercial complexes as well as the utilisation of more energy efficient processes and technologies. A project on the development of an energy efficiency strategy was carried out to evaluate the legal, regulatory and financial framework with the aim of promoting the efficient utilisation of energy.²

The Ninth Malaysia Plan

Efforts were continued in the Ninth Malaysia Plan (“the 9MP”) to promote the utilisation of renewable energy resources. Under the Small Renewable Energy Power (or SREP) programme, two projects with a combined grid connected capacity of 12MW were implemented. A roadmap for the development of solar, hydrogen and fuel cells was formulated.

In terms of energy efficiency, the focus was on the design and installation of energy efficient features in government buildings. Thus, new guidelines on energy efficiency designs for clinics and schools were formulated. Energy audits were also undertaken in eight energy-intensive industries under the Malaysian Industrial Energy Efficiency Improvement Project (or MIEEIP) to identify potential energy savings.³

¹ According to the Intergovernmental Panel on Climate Change (source: Wikipedia)

² 8MP (2001-05), p 324

³ 9MP (2006-10), p 401

Fiscal incentives

The Malaysian government provided fiscal incentives to stimulate the emergence of renewable energy and energy efficiency projects. For instance, companies generating energy from renewable sources enjoy import duty and sales tax exemption on imported equipment used to generate energy from renewable sources, and sales tax exemption on equipment purchased from local manufacturers.⁴

Companies providing energy conservation services or incurring capital expenditure for energy conservation for their own consumption enjoy import duty and sales tax exemption on energy conservation equipment that is not produced locally.⁵

Kyoto Protocol

In order for environmental stewardship to be promoted continually to ensure that the balance between development needs and the environment is maintained, the Malaysian government took the initiative to ratify the Kyoto Protocol, and hence committed to reduce greenhouse gas (“GHG”) emissions to about 5% by 2012.

To reduce GHG emissions, developing countries can either restructure their operations to cut carbon dioxide (“CO₂”) emissions or buy carbon credits from companies or countries that have spare carbon credit allowances under the Clean Development Mechanism (“the CDM”), an important feature of the Kyoto Protocol.

To reduce GHG emissions, developing countries can either restructure their operations to cut carbon dioxide emissions or buy carbon credits from companies or countries that have spare carbon credit allowances under the Clean Development Mechanism.

Two major agreements were adopted by the international community: the United Nations Framework Convention on Climate Change (“the UNFCCC”) in 1992 in Rio and, more recently, its principal update, the Kyoto Protocol, in 1997. While the UNFCCC is aimed at stabilising

GHG concentrations in the atmosphere, it sets no mandatory limits on GHG emissions for individual countries and contains no enforcement provisions.

In contrast to the UNFCCC, the Kyoto Protocol sets quantified and binding commitments for limiting or reducing GHG emissions of anthropogenic origin for countries that are developed or in the transition process towards a market economy, for the 2008-12 commitment periods. These countries are referred to as Annex I parties.

Developing countries do not have any legally binding targets under the Kyoto Protocol. The countries without any targets are known as Non-Annex I parties, one of which is Malaysia.

Clean Development Mechanism

The Kyoto Protocol has three market mechanisms that can be used to meet targets: joint implementation (JI), international emissions trading (IET) and the Clean Development Mechanism (“CDM”). Among the three, only CDM aims

⁴ See 2009 Budget Commentary & Tax Information by the Malaysian Institute of Accountants, the Malaysian Institute of Certified Public Accountants and the Malaysian Institute of Taxation, at p 48

⁵ See 2009 Budget Commentary & Tax Information by the Malaysian Institute of Accountants, the Malaysian Institute of Certified Public Accountants and the Malaysian Institute of Taxation, at p 49

to promote co-operative measures between industrialised/developed (Annex I) and developing (Non-Annex I) countries.

The CDM was proposed with the twin objectives of helping Annex I countries achieve their emission reduction targets and, at the same time, assist non-Annex I countries in promoting sustainable development in their economies.

Its thrust is to facilitate co-operative projects between developed and developing countries for the reduction of GHG emissions, with the opportunity for additional financial and technological investments in GHG reduction projects.

The CDM seeks to help developed countries achieve their emission reduction targets and, at the same time, help developing countries promote suitable developments in their economies.

The GHG emission reduction achieved by the CDM project will be quantified in standard units known as “Certified Emission Reductions” (“CERs”), which can be traded and used by the buyers to meet their emission reduction targets. It involves the trading of emission reductions that are resulting from a specific project to countries that can use these CERs to meet their emission reduction targets.

Using this approach, the CDM creates a win-win relationship between industrialised and developing countries. In return for the CERs, there will be a transfer of money to the project that actually reduces the GHGs.

GHG reduction in Malaysia

Projects that have the potential to reduce GHG in Malaysia include:

- Renewable energy projects, encompassing photovoltaic, hydro and biomass;
- Industrial energy efficiency;

- Supply and demand side energy efficiency in the domestic and commercial sectors;
- Landfill management (flaring or landfill gas to energy);
- Combined heat and power projects;
- Fuel switch to less carbon intensive fuels (e.g. from coal to gas or biomass);
- Biogas to energy (from palm oil mill effluent or other sources);
- Reduced flaring and venting in the oil and gas sector;
- Land-use, land-use change and forestry projects (afforestation, reforestation, forest management, cropland management, grazing land management and re-vegetation).

National CDM guidelines

The national guidelines on CDM issued on 18 August 2005 require that CDM projects meet five criteria:

- (i) the projects must support sustainable national development. Various economic, ecological and social aspects have to be taken into account;
- (ii) participation of a partner from an Annex I country has to be ensured;
- (iii) a transfer of technology or an improvement in current technologies;
- (iv) the CDM executive board must examine whether the project fulfils the requirements; and
- (v) the applicant must demonstrate its ability to carry out the project. To be eligible, a locally incorporated company in Malaysia with a minimum paid-up capital of RM100,000 must have been formed, and it has to provide evidence of project finance.

At present, tax incentives are available for companies that carry out activities relating to environment management, which include recycling of agricultural waste into value-added products, generation of renewable energy sources and energy conservation projects.

All these activities have the potential to obtain CERs of the CDM projects. A pertinent provision of the 2008 Budget, though yet to be gazetted, provides that companies that have been successful in reducing emission of GHG and granted tradable CER certification be given tax exemption on the income derived from the trading of CER certificates.⁶

Financial incentives

From a corporate perspective, the main incentive to go green would be that such a practice constitutes good corporate social responsibility as well as the cost recovery potential. When companies introduce CDM projects to their businesses, they would have to buy machinery or carry out operations that emit lower levels of carbon dioxide. That would give them excess carbon credit that can be sold to other companies in need of the credit. Hence the cost of going green would then be compensated.

According to Pusat Tenaga Malaysia, agricultural and natural resources-rich Malaysia has potential of up to 100 million tonnes of CO₂ equivalent, for the period 2006 to 2012 (assuming an annual potential of 18 million CERs per year in 2010). The market price is between US\$3 and

US\$10 per tonne, which corresponds to a total capital inflow of RM1.14 billion to RM3.8 billion for Malaysia from the sale of CERs.

Bilateral and multilateral CDM projects might typically leverage project financing three to four times this amount, hence contributing substantially to foreign direct investment and technology transfer.

The first Malaysian CDM project is Biomass Energy Plant Lumut, developed by ENCO Energy. It involved the installation of a modern and efficient biomass-fired cogeneration system to supply steam and electricity to the PGEO palm oil refinery in Lumut, Perak. It is expected to reduce 200,000 tonnes of CO₂ between 2006 and 2012. The

purchaser of the CDM credits is the Danish Ministry of Foreign Affairs.

Business opportunities

Up until last September, the CDM executive board had registered a total of 32 projects from Malaysia with an estimated annual reduction of 2.56 million tonnes of CER.

Another 90-odd projects are under evaluation. Measured by the number of registered projects worldwide, Malaysia was ranked No.5 (world market share: 2.8%) and No.8 (share: 1.15%) by anticipated resulting annual CERs. To date, Malaysia can account for approximately 600,000 tonnes of CERs.

From a corporate perspective, the main incentive to go green would be that such a practice constitutes good corporate social responsibility as well as the cost recovery potential.

⁶ See 2009 Budget Commentary & Tax Information by the Malaysian Institute of Accountants, the Malaysian Institute of Certified Public Accountants and the Malaysian Institute of Taxation, at p 58

Elsewhere, the emission reductions from ongoing activities have so far largely been acquired by buyers from Denmark, Canada, Japan and Switzerland. Besides government buyers, private companies such as Germany's Vattenfall Europe Generation and Canada's Pathgreen Investment Ltd are also actively scouting for new CDM project potential.

Foreign direct investments include investments from Australia, Taiwan, Britain, Singapore and Germany.

A Singapore firm, Agni Inc Pte Ltd, recently won its second biomass power plants contract in Malaysia from Wilgate Sdn Bhd to design, build and commission two renewable energy power plants.

DiGi Telecommunications Sdn Bhd has committed to invest up to RM100 million in its Deep Green programme, for which it will spend RM50 million to RM100 million over the next three years. Deep Green is aimed at reducing the company's carbon footprint by half in 2012.

Funds available for green investments

A substantial portion of the publicly known capital for purchasing carbon emission reductions comes from funds and multilateral buyers. Major institutional buyers include government and private sector carbon funds.

Government carbon funds

- World Bank's Prototype Carbon Fund
- CAF (by Andean Development Corporation)
- IFC-Netherlands Carbon Facility (INCaF)
- Development Bank of Japan

- Japan Bank for International Cooperation (JBIC)
- KfW Bankengruppe
- The Netherlands Clean Development Facility.

Private sector carbon funds

- European Carbon Fund (ECF)
- EcoSecurities Standard Bank Carbon Facility
- Greenhouse Gas-Credit Aggregation Pool (GG-CAP) (by Natsource Asset Management Corporation)
- Rabo Bank
- ICECAP (sponsored by Cumbria Energy Limited and Investec Bank UK)
- Asia Carbon Fund
- Climate Investment Partnership
- Japan Greenhouse Gas Reduction Fund (JGRF).

Green Building Index

Green Building Index Malaysia was introduced on 3 January 2009 by the Malaysian Institute of Architects and the Association of Consulting Engineers. The green rating tool is intended to promote sustainability in the built environment and raise awareness of environmental issues among developers, architects, engineers, planners, designers, contractors and the public.

The rationale behind designing a green building is to:

- save energy and resources, recycle materials and minimise the emission of toxic substances throughout its life cycle;
- harmonise with the local climate, traditions, culture and the surrounding environment; and
- be able to sustain and improve the quality of human life while maintaining the capacity of the ecosystem at local and global levels.

Examples of green building features (using a combination of energy efficiency, renewable energy and conservation technologies) are:

- Sensor-controlled and compact fluorescent lighting
- High-efficiency heat pumps
- Geothermal heating (temperate countries)
- Building integrated photovoltaic system
- Solar thermal tubes
- Solar chimneys
- On-site cleaning
- Reuse of wastewater
- Building orientation
- Radiant cooling systems that take advantage of naturally occurring conditions
- Salvaged lumber products
- Recycled concrete aggregates
- Green roof and rainwater collection
- Waterless urinals
- Facilities of bicyclists
- Permeable pavers, cork floors and use of local products.

GBI assessment framework

The evaluation process involves an assessment during the design stage leading to the award of the provisional GBI Malaysia rating. The final award is given one year after the building is first occupied.

There are four categories of rating: platinum, gold, silver and certified. The rating will be reviewed every three years to ensure that such green buildings are well maintained and operated in accordance with their design. As such, tenancy agreements and leases should provide for the obligations of the landlord and the tenant/lessee to maintain and upkeep the building as a green building and in compliance with the requirements of the GBI rating tool. **LH-AG**

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Industrial Building Allowance for Hotels: A Legal Analysis of s.30 of the Promotion of Investments Act 1986*

by Datuk D P Naban and S Saravana Kumar

Let's say Maju Sdn Bhd owns and manages Hotel Five Star, which is registered with the Ministry of Tourism. Since the tourism industry in Malaysia appeared to be thriving, the company decided to expand and modernise its hotel business by constructing a 10-storey block with 200 guestrooms, three function rooms and a banquet hall. It also decided to renovate the existing hotel building.

The company applied for investment tax allowance, which was approved by the Ministry of International Trade and Industry on 2 January 1994 for a period of five years, effective from 2 January 1992. The total investment tax allowance is 60% of the capital expenditure incurred.

As the company was granted investment tax allowance, it was also entitled to industrial building allowance from the year of assessment 1993. The investment tax allowance ceased on 1 January 1997.

The company continued to claim industrial building allowance on the residual value of the capital expenditure incurred although the investment tax allowance had expired. The Inland Revenue Board ("the IRB") disallowed this on the premise that since the investment tax allowance had expired, Maju was no longer entitled to industrial building allowance.

Is the IRB's approach correct?

Currently, a building used as a hotel is treated as an industrial building and is eligible

for industrial building allowance. This was made possible by an amendment¹ to the Income Tax Act 1967 ("the ITA"), which introduced a new para 37F to Schedule 3. Paragraph 37F reads as follows:

"The provisions of this Schedule relating to industrial buildings shall apply, *mutatis mutandis*, to a building or part thereof used by a person solely for the purpose of an hotel and that hotel is registered with the Ministry of Tourism."

Prior to para 37F, as a general rule a building used as a hotel was not to be treated as an industrial building and did not qualify for industrial building allowance.² However, there are two exceptions to this rule, made available by ss.19 and 30 of the Promotion of Investments Act 1986 ("the PIA"), whereby industrial building allowance is available for the hotel building of a company which either enjoys pioneer status or investment tax allowance.³

Although ss.19 and 30 of the PIA prescribe the circumstances in which a company is entitled to industrial building allowance for its hotel building, the provisions are silent as to the duration for which such company may enjoy that allowance. Thus, the question arises as to whether the availability of industrial building allowance is limited only to the duration in which a company enjoys pioneer status or investment tax allowance.

This article aims to discuss this anomaly but the authors will be focusing on s.30 of the PIA only. In that regard, this article analyses s.30 with the view of determining whether a company may

* This article was first published in Tax Guardian (Vol 2/No 1/2009/Q1), which is the official journal of the Malaysian Institute of Taxation.

1 Paragraph 37F was first inserted under s.8 of the Finance Act 2002. It was subsequently amended under s.31 of the Finance Act 2006, where the words "Culture, Arts and" were deleted from the original provision.

2 See para 65(3), Schedule 3 of the ITA, which read as follows before amendment in 2002:

Subject to paragraph 67B, a building used as a dwelling house (not being for accommodation of the kind mentioned in sub-paragraph (2)) or a retail shop, showroom, hotel or office is not and shall not be treated as an industrial building.

3 Provided the conditions in para 37F of Schedule 3 are met, a hotel building qualifies as an industrial building today, notwithstanding whether the company owning the hotel is granted pioneer status or investment tax allowance.

continue to claim industrial building allowance on the residual value⁴ of the hotel's qualifying capital expenditure even after the expiration of investment tax allowance.

There are two schools of thought on this matter. The first (contended more frequently by the IRB) is that the availability of industrial building allowance is limited to the duration in which a company enjoys investment tax allowance. This means industrial building allowance is only available for five years (i.e. the duration of investment tax allowance) and there is no industrial building allowance on the residual value of the hotel's qualifying capital expenditure.

The second view is that once industrial building allowance is granted, it continues to be available on the residual value of the qualifying capital expenditure, notwithstanding the expiration of the investment tax allowance.

In order to ascertain the correct position, the authors propose that one examines:

- (a) the provisions of the PIA;
- (b) the purpose of the PIA and the purposive approach;
- (c) whether industrial building allowance is available until it is exhausted; and
- (d) the ambiguity in interpretation.

Section 30 of the PIA reads:

“Where an hotel business is carried on in Malaysia by a company granted an approval under section 27 in a hotel building of the approved standard or in the extended or modernized part of an existing hotel building where such extension or modernization is of

an approved standard, **section 19 shall apply, *mutatis mutandis*, to that hotel building or such extended or modernized part thereof** (authors' emphasis).”

(a) *Provisions of the PIA*

Section 19(1) reads:

“Where a company has incurred capital expenditure on a hotel building of the approved standard in Malaysia or incurred capital expenditure in extending or modernizing an existing hotel building to the approved standard in Malaysia, and a hotel business is carried on in that building by a pioneer company, such hotel building or such extended or modernized part thereof, as the case may be, shall notwithstanding subparagraph 65 (3) of Schedule 3 to the principal Act be deemed to be an industrial building for the purpose of that Schedule:

Provided that where the defined authority is not satisfied that the hotel building, including any extended or modernized part thereof, is maintained to the approved standard in a basis period for a year of assessment, that building or the extended or modernized part thereof shall cease to be an industrial building for that year of assessment and subsequent years of assessment.”

Meanwhile, s.30 of the PIA states that s.19 shall apply *mutatis mutandis* to a company granted an approval under s.27(1) of the PIA.⁵

Section 19(1) of the PIA provides that where a hotel business is carried on in a building by a pioneer company, such hotel building is deemed

⁴ Currently, the industrial building allowance rate is 3% per annum.

⁵ Section 27(1) of the PIA reads:

The Minister may grant approval in respect of an application for an investment tax allowance made under subsection 26(1) subject to such terms and conditions as he deems fit, and such approval may be granted retrospectively from a date not earlier than the date from which the activity or the product has been determined to be a promoted activity or a promoted product under section 4.

to be an industrial building and is eligible for industrial building allowance notwithstanding subpara 65(3) of Schedule 3 of the ITA, provided the capital expenditure was incurred:

- (i) on an hotel building of the approved standard in Malaysia; or
- (ii) in extending or modernizing an existing hotel building to the approved standard in Malaysia.

The better view is that the words “pioneer company” in s.19 are to be changed to “a company which is granted an approval under Section 27” by reason of s.30 of the PIA.

Meanwhile, the word “hotel” is defined under s.2 of the PIA as any accommodation, which includes a hotel, a motel, chalet or hostel, of the approved standard registered with the Ministry of Tourism.

“Approved standard”,⁶ in relation to a hotel, means the standard as determined by the defined authority. The “defined authority”⁷ is the Minister of International Trade and Industry with the concurrence in writing of the Minister of Finance.

Sections 19, 27 and 30 of the PIA are silent as to whether industrial building allowance expires upon the expiration of investment tax allowance. Literal construction is the normal method that is employed to construe or interpret a legal provision or statute.

In this regard, applying the literal construction to s.30, the authors are of the view that once investment tax allowance is granted, hotels are entitled to industrial building allowance. Further, the general principle is that the industrial building allowance is available until it has been exhausted.⁸

Therefore, had Parliament intended the industrial building allowance to be restricted only to the period in which investment tax allowance is applicable, then Parliament would have specified this clearly in the PIA, especially in s.30.

(b) Purpose of the PIA and the purposive approach

The PIA, which was first introduced in 1986, was part of the tax incentive measures by the government to promote and stimulate industrialisation and manufacturing as the core of the Malaysian economy. The purpose of PIA received judicial notice in *Director General of Inland Revenue v Sebangun Sdn Bhd*,⁹ where the High Court observed:

“In the early 1980s the Government in its effort to turn the economy of the country from an agricultural based to that of industrialisation had introduced many novel things or steps; and some of which were taken through legislation. Thus in pursuance of this policy that the Promotion of Investments Act 1986 was conceived, which replaced the Investment Incentive Act 1968 and which makes provision for promotion by way of relief from income tax the establishment and development in Malaysia of industrial, agricultural and other commercial enterprises, the promotion of exports or incidental and related purposes.”

In *Sebangun*, the High Court, in considering the meaning of “manufacture” pursuant to s.36(1) of the PIA, held that the word must be given the meaning that Parliament intended it to mean; that is to say, it must be interpreted in the spirit and intendment of the legislation. In deciphering

⁶ See s.2 of the PIA

⁷ See s.2 of the PIA

⁸ See *GASMSB v Ketua Pengarah Hasil Dalam Negeri* [1996] 1 BLJ 358 and the discussion below

⁹ [1997] 3 AMR 3101

Parliament's intention, the High Court commented that it is necessary in seeking the intention of the legislation that one has to trace it from its beginning, i.e. the inception of the Act.

The authors would like to add that following the case of *Sebangun* in interpreting s.30 of the PIA, besides using literal construction, one may also consider the purpose of Parliament in legislating the Act or sections. The granting of the investment tax allowance and industrial building allowance is consistent with the objectives of the PIA to promote industrialisation as the catalyst to boost economic development.

In this regard, can Parliament be said to have only intended to grant industrial building allowance for a hotel for a period of five years, i.e. only as long as the hotel was enjoying the investment tax allowance?

The authors submit that since the purpose of the PIA is to promote economic development by way of tax incentives, Parliament would not have taken such a restrictive view. Therefore, that the industrial building allowance is available until it is exhausted is the preferred view.

In addition, the application of a purposive approach to construe s.30 of the PIA is in accordance with s.17A of the Interpretation Acts 1948 and 1967. The purposive approach was applied to interpret tax statutes by the Federal Court in *Palm Oil Research and Development Board Malaysia & Anor v Premium Vegetable Oils Sdn Bhd*.¹⁰

Since Parliament did not expressly limit the period for which industrial building allowance is available, to include such limitation period to ss.19

and 30 of the PIA would be akin to re-writing the provisions. Gopal Sri Ram JCA (as he then was) in *Palm Oil Research and Development Board Malaysia* commented:

“If this court were to accept the argument of counsel for the appellant, then we would not be promoting the purpose or object of the 1979 Act [Palm Oil Research and Development Act] but be defeating it. For, in such event, we would, through unauthorised legislative power, be re-writing statute.”

Interestingly, in *South India Paper Mills Ltd v Director of Inspection and Audit (Customs and Central Excise) and Anr*,¹¹ the Indian High Court held that:

“When Parliament has not prescribed any period of limitation for claiming the benefits under this chapter it is not open to the Central Govt. to transgress beyond its power to prescribe the time limit in order to avail of the benefit of the scheme.”

In these circumstances, the authors respectfully submit that the IRB cannot act beyond its power to prescribe the time limit for which industrial building allowance is to be allowed. Therefore, the entitlement of industrial building allowance shall not be restricted to the duration of investment tax allowance alone.

(c) Whether industrial building allowance available until it is exhausted

Further, s.1(2) of the PIA states that the Act shall be read and construed as one with the ITA. In this regard, the industrial building allowance will be regulated pursuant to Schedule 3 of the ITA. The position under Schedule 3 is that industrial building allowance will last for a period of 30

¹⁰ [2004] 2 CLJ 265

¹¹ [1984] 145 ITR 194

years (with an initial allowance of 10% and annual allowance of 3%).

In *GASMSB v Ketua Pengarah Hasil Dalam Negeri*,¹² the Special Commissioners stated that:

“The allowances are calculated by reference to the estimated useful life of the asset which is reflected in the rates prescribed by the Director General of Inland Revenue. The allowances commence in the year when the expenditure is incurred and continue to be given in subsequent years until the qualifying expenditure is fully set off or the asset is disposed. The allowances due for each year of assessment are calculated on the written down value or residual expenditure of the asset.”

Although *GASMSB* concerns the issue on capital allowance, the principle stated in that case is also the general position under Schedule 3 for industrial building allowance. This clearly supports the authors’ contention that the industrial building allowance is available until it is fully exhausted.

This is because, if the interpretation contended by the IRB is correct, it would mean a hotel is only entitled to claim a total of 25% (initial allowance of 10% and 3% allowance for the five years) of the total industrial building allowance. This certainly cannot be the intention of Parliament.

In legislating and introducing industrial building allowance via s.30 of the PIA, Parliament would have certainly known it will take a hotel 30 years to exhaust the allowance granted to it. This construction finds support from the following observation made by the High Court in *Sebangun*:

“In *Lim Phin Khian v Kho Su Ming* [1996] 1 MLJ 1 the Federal Court said that there is an un rebuttable presumption Parliament is

presumed to know all the relevant law upon the particular subject upon which it legislates. The correct approach is to look at the substance and general purpose of the legislation in order to discover its objective aim or general purpose.”

In this regard, given that:

- (i) Parliament is presumed to know that it will take hotels 30 years to exhaust the industrial building allowance; and
- (ii) the intention of Parliament in legislating the PIA is to promote economic development by way of tax incentives,

it is logical to contend that the industrial building allowance granted to hotels does not cease upon the expiration of investment tax allowance. Had Parliament intended otherwise, it would have been expressly prescribed in s.30 of the PIA, or Parliament would have provided for accelerated industrial building allowance, which would enable hotels to exhaust the allowance in five years like investment tax allowance. Hence, pursuant to Schedule 3 of the ITA and the observation made by the Special Commissioners in *GASMSB*, it is only logical that a hotel is entitled to claim industrial building allowance until the total qualifying capital expenditure has been exhausted.

In addition, it has also been recognised by the Malaysian Industrial Development Authority (“MIDA”), one of the authorities established by the Ministry of International Trade and Industry, that industrial building allowance is available until fully exhausted. In one of MIDA’s booklets, it is stated that:

“An industrial building allowance is granted to companies incurring capital expenditure on the construction or purchase of a building

¹² [1996] 1 BLJ 358

that is used for specific purposes, including... hotels that are registered with the Ministry of Tourism. Such companies are eligible for an initial allowance of 10% and an annual allowance of 3%. As such, the expenditure can be written off in 30 years.”¹³

This shows that it is the intention of Parliament that industrial building allowance is available until it is fully exhausted, and there is no time restriction for a hotel to claim industrial building allowance.

(d) *Ambiguity in interpretation*

Notwithstanding the above, in the event that there is any doubt on the interpretation of s.30 of the PIA, it should be resolved in favour of the hotels. In *National Land Finance Co-operative Society Ltd v Director-General of Inland Revenue*,¹⁴ the Supreme Court held that in the event that there is a doubt in any legislation regarding Parliament’s intention, the ambiguity must be construed in favour of the taxpayer, i.e. the hotels. Gunn Chit Tuan CJ (Malaya) commented:

“The provisions of the Act [Income Tax Act 1967] must be construed having regard to the Interpretation Acts 1948 and 1967. There is therefore a doubt whether the legislature had intended to impair the existing right of the taxpayer and inflict a detriment to it as it takes away a vested right under the existing law to exemption from tax. As there is a doubt, the ambiguity must be construed in favour of the taxpayer as the said exemption from tax has not been removed by sufficiently clear words to achieve that purpose.”

Conclusion

For the reasons articulated above, hotels are entitled to continue claiming industrial building allowance under s.30 of the PIA on the residual value of the qualifying capital expenditure until it has been fully utilised, even if the investment tax allowance granted under s.27 of the PIA has already expired.

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¹³ See p 17 of *The Guide for Malaysian Manufacturers (Book 3)*, MIDA (April 2007)

¹⁴ [1994] 4 BLJ 33

Facilitating Greater Access to the Capital Market

by Mohd Khairil Ezane Azman

The global financial crisis has been cited as one of the factors for the poor performance of Bursa Malaysia Securities Berhad (“Bursa Securities”), a subsidiary of Bursa Malaysia that provides, operates and maintains the main securities exchange in Malaysia. The crisis has also adversely affected investor and consumer sentiment.

To mitigate the impact of the crisis on the country, a RM60 billion mini budget was announced by finance minister (also then deputy prime minister) Datuk Seri Najib Tun Razak on 16 March 2009. Notably, one of the measures is to facilitate better access to the capital markets in Malaysia.

This called for some relaxation of the existing regulatory provisions involving the Securities Commission as outlined below.

Rights issues by listed companies

Rights issues by listed companies no longer need the approval of the Securities Commission (“the SC”). According to its chairman Datuk Seri Zarinah Anwar, rights issuance may be on the uptrend in 2009 as listed companies seek funds from investors who are already familiar with the particular company’s business.¹

In light of the current aversion to risk in the market, presumably it would be easier for companies to raise funds from investors who have intimate knowledge of their financial footing and plans in moving forward.²

The liberalisation is timely, but given the poor condition of the equities and bond markets in Malaysia, it remains to be seen whether

such a move would encourage greater investor involvement and actually spur more companies to undertake rights issues.

Revision of terms and conditions of bonds and Sukuk

A revision to the terms and conditions of bonds or Sukuk already approved by the SC, pursuant to s.212 of the Capital Markets and Services Act 2007³ (“the CMSA”) and already issued, no longer requires approval from the SC.

However, the SC should still be notified of the changes by the principal adviser. He must ensure the revision meets prerequisites such as obtaining the consent from bond/Sukuk holders and other relevant parties, and making sure material information pertinent to the revision, including the impact on credit rating and the Shariah adviser’s opinion on the proposed revision, have been communicated and disclosed to the bond/Sukuk holders.

Communication to FAST

Two separate announcements must be made on the Fully Automated System for Issuing/Tendering (“FAST”);

- one on the proposed revision (to be announced on FAST prior to obtaining the approval of the bond/Sukuk holders); and
- one on the outcome of the bond/Sukuk holders’ decision (to be announced on FAST immediately after the bond/Sukuk holders have decided on the proposed revision).

The announcement on FAST regarding the proposed revision must be copied to the SC within

¹ ‘Rights issue on an uptrend, says SC’ (*Daily Express*, 12 March 2009: www.dailyexpress.com.my/news.cfm?NewsID=63416)

² ‘Rights issue on an uptrend, says SC’ (*Daily Express*, 12 March 2009: www.dailyexpress.com.my/news.cfm?NewsID=63416)

³ Act 671. Section 212 concerns proposals to be submitted to the Securities Commission.

the same day of announcement. Announcements on FAST are not applicable to bonds/Sukuk (including loan stocks) that are listed and traded on Bursa Malaysia.⁴

The cost payable to the SC for revision to the terms and conditions of the bonds and Sukuk that complies with the above would not be applicable. However, SC approval is still necessary for applications to increase the size of bonds and Sukuk, as well as for proposals to revise the principal terms and conditions of bonds and Sukuk that have been approved by the SC but not yet issued.

Revision of bonds and Sukuk for listing on Bursa Malaysia

In December 2008, Bursa Securities introduced a framework in support of the initiative of the Malaysia International Islamic Financial Centre (MIFC) to position the country as a leading market for the issuance and distribution of Sukuk.

The framework allows issuers to list their bonds and Sukuk without them being quoted and traded on the Malaysian bourse. In this regard, Sukuk and bonds can still be issued through FAST and transacted under the Real Time Electronic Transfer of Funds and Securities (RENTAS) system.

Revision of the existing terms and conditions of bonds and Sukuk to comply with Bursa Malaysia's Listing Requirements need only be notified to the SC. This applies to all bonds and Sukuk.

This new measure benefits the issuer of bonds and Sukuk for it would no longer need to prepare

applications on revision for the SC's approval. Previously, such applications usually took two weeks for the SC to process. The new mechanism for the revision would save both time and cost for the issuer.

Issuance and offering of equity securities by unlisted public companies

Unlisted public companies are now exempted from having to obtain SC approval for the issuance or offering of equity securities. This is a boost for secondary equity fund raising and corporate activities.

Following the exemption, an issuance exercise should be completed within nine weeks inclusive of getting shareholders' approval and issuing the abridged prospectus. In addition, the cost of undertaking the rights issue will now be much lower; for example, the fees payable to the SC for rights issue (RM15,000 + 0.05% of the nominal share value) have been removed.⁵

This exemption does not jeopardise the rights of shareholders as the rights issues would still require their approval. All shareholders are equal and have the right to participate in the exercise.

The standard of disclosure is maintained as the SC will continue to register prospectuses for such rights issues and it has the power to act against non-compliance.

However, the exemption is not applicable to structured warrants and proposals by foreign unlisted public companies, unless already exempted under s.213 of the CMSA.⁶

4 SC press release on 16 March 2009, "New measures to facilitate greater access to the capital market" (www.sc.com.my)

5 SC press release on 16 March 2009, "New measures to facilitate greater access to the capital market" (www.sc.com.my)

6 Classes or categories of transactions or securities not subject to subsection 212(4)

Malaysian Code on Take-Overs and Mergers 1998

The Malaysian Code on Take-Overs and Mergers 1998 (“the Code”) came into operation on 1 January 1999. Its purpose is to regulate and administer the conduct of all parties involved in a take-over, merger or compulsory acquisition.

Although the Code was meant for public listed companies, by virtue of Practice Note 1.2, applicability was extended to private limited companies having shareholders’ funds or paid-up capital of RM10 million or more based on the latest audited account, or where the purchase consideration is not less than RM20 million.

Under the proposed new measure to facilitate greater access to the capital market, the Code will no longer apply to private limited companies. However, the control of a public company through an acquisition or control by a private company would still be subjected to the Code.

It is arguable that the rights of shareholders are protected due to the small number of shareholders in a private company. The intention of the measure may be that it will provide greater flexibility and benefit private companies in restructuring or expanding the company’s business more efficiently.

Removal of mandatory credit rating requirement for convertible and exchangeable bonds and Sukuk

The rating of bonds is compulsory under paragraph 7.0 of the Guidelines on the Offering of Private Debt Securities.⁷ The existence of mandatory credit rating in Malaysia is the result of

an emerging debt market where investors are less sophisticated and disclosure standards are low.⁸ Once a rating is assigned, the rating agency will monitor the rating throughout the life of the rated instrument.

A rating agency may publish a “rating alert” to inform the market of developments that may have an impact on the status of the rated instrument, for example, a proposed merger or take-over, changes in government policies, economic environment and the like. Subsequently, the rating would either be revised or reaffirmed.⁹ Nevertheless, the ultimate accuracy of rating is always difficult to evaluate as it is only tested on maturity.¹⁰

The recent mini budget in Malaysia exempts the following from the mandatory credit rating requirement:

- (a) where the investors of the bonds/Sukuk or loan stocks are given the right to convert or exchange the bonds/Sukuk or loan stocks into the underlying shares during the tenure of such issue; and
- (b) the underlying shares are listed on a security exchange.

For the existing issues of convertible and exchangeable bond/Sukuk that are currently rated, an issuer would require the bond/Sukuk/loan stock holders to consent to the removal of the rating requirement. Nevertheless, investors still have the right to request the issuer to undertake credit ratings.

As the Malaysian securities market is moving in stages towards a disclosure-based system, the initiative would enable well-known, lower-risk

⁷ Securities Commission. 2004

⁸ [2002] JMCL 4; (2002) 29 *Journal of Malaysian and Comparative Law* 83

⁹ [2002] JMCL 4; (2002) 29 *Journal of Malaysian and Comparative Law* 83

¹⁰ [2002] JMCL 4; (2002) 29 *Journal of Malaysian and Comparative Law* 83

corporations to issue bonds without a credit rating if they so choose. Nevertheless, market pricing would normally favour bond issues with known credit ratings as most investors rely on credit ratings in determining the level of risk and the expected returns for their investment.

Revised guidelines for structured warrants

The SC released a revised set of guidelines governing the issuance of structured warrants, which took effect on 8 May 2009. Chapter 5 of the Listing Requirements of Bursa Malaysia was amended to give effect to the revision.

Significant changes to the guidelines include:

- (a) allowing the issuance of structured warrants on foreign and local exchange-traded funds;
- (b) allowing issuers to boost liquidity via market making in lieu of the spread requirement;
- (c) for the purpose of market making, allowing issuers to apply for a further issue of structured warrants within the existing issue; and
- (d) introducing a minimum issue price of 15 sen after taking into account minimum trading costs.

For details on the structured warrants guidelines, log on to www.sc.com.my/eng/html/resources/guidelines/structuredwarrants/gl_structuredwarrants_090508.pdf and

www.sc.com.my/eng/html/resources/guidelines/structuredwarrants/faq_structuredwarrants_090508.pdf.

The additional measures related to the capital market will certainly promote greater efficiency and allow listed issuers to raise additional funds expeditiously.

LH-AG

NB: The initiatives on revisions to the terms and conditions of bonds and Sukuk as well as the exemption from the mandatory credit rating requirement for convertible and exchangeable bonds and Sukuk announced in the second stimulus package took effect on 16 March 2009. The exemptions on the other initiatives will take effect following the gazette of a ministerial order, which will be made known later.

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Case Note

Dato' Anthony See Teow Guan v See Teow Chuan & Anor [2009] 3 MLJ 14 (FC)

Legal professional privilege and confidentiality

In Malaysia, legal professional privilege is enshrined in sections 126 to 129 of the Evidence Act 1950 (“the Act”), which deal with what witnesses may or may not say, and with their privileges and immunities.

Section 126 governs a situation where a lawyer is a witness and it forbids him from disclosing any communication made to him by or on behalf of his client or any advice given by him to the client. There is only one exception where the privilege does not apply – when the client gives his express consent to the advocate who is called as a witness to make the disclosure.

The parties to this case were directors and shareholders of Kian Joo Holdings Berhad, which had a stake in public listed Kian Joo Can Factory Berhad (“the company”). STG was the executive director and general manager of the company (“the GM”) while two of them, STC and STK (“the plaintiffs”), were the managing director and executive director/factory manager respectively.

The GM and the company’s financial controller instructed an advocate and solicitor (“the advocate”) to advise on the plaintiffs’ operating another company, KLMP. Acting on information provided by the GM and the financial controller, the advocate drew up a legal opinion addressed to the company for the GM’s attention. The legal opinion was seen by various persons, and the plaintiffs received a copy from two external auditors.

The plaintiffs instituted defamation proceedings against the GM following the publication of the legal opinion, alleging that it was defamatory because it contained allegations that they were dishonest and had acted in breach of their duties as

directors of the company by siphoning money away from it and raising fictitious invoices in favour of KLMP.

When the plaintiffs sought to admit the legal opinion at trial, the advocate, who was called as the first witness, said she was unable to answer any questions on the legal opinion by reason of legal professional privilege.

At the conclusion of a trial within a trial to determine the admissibility of the legal opinion, the High Court agreed with the advocate that she could not be compelled to disclose the communications she had with the GM, and held that the legal opinion could not be produced in evidence on the grounds of advocate-client privilege.

The Court of Appeal reversed the decision and held that the GM had waived the confidentiality and privilege attached to the legal opinion, and that protection under s.126 did not apply to the communication between the GM and the advocate.

The GM was granted leave to appeal to the Federal Court on nine questions relating to:

- (i) privilege and confidentiality;
- (ii) waiver and express consent;
- (iii) disclosure and third parties;
- (iv) discovery under O.24 of the Rules of the High Court 1980 (“the RHC”).

The Federal Court allowed the appeal and set aside the decision of the Court of Appeal. A summary of the findings of the Federal Court on these points follows below.

(i) Privilege and confidentiality

The common law maxim “once privileged, always privileged” is embodied in sections 126 to 129 of the Act. The privilege is absolute and remains

so until it is waived by the privilege holder, i.e. the client. The sole exception where the privilege does not apply is when the client gives his express consent to the advocate who is called as a witness to make the disclosure.

The Federal Court held that the exception under s.126 is concerned with whether the privilege holder is prepared to waive the privilege for court proceedings. It is the privilege that has to be waived, not the confidentiality.

(ii) *Waiver and express consent*

The Federal Court held that “express consent” meant that there must be an intentional and deliberate act to waive the legal privilege by the privilege holder. Since the company was the client of the advocate, and not the GM, the company was the privilege holder. It was for the company to decide whether or not to waive the privilege and to convey the consent to the advocate when the latter was called to give evidence.

The advocate was right to refuse disclosure of the legal opinion by reason of privilege under s.126. She was acting on behalf of the company and therefore duty bound to support the privilege accorded to the organisation. It followed that the High Court was correct to disallow disclosure of the legal opinion through the advocate on the grounds of privilege and in holding that there was no express consent by the company for the advocate to waive the privilege.

(iii) *Disclosure and third parties*

The Court of Appeal ruled that privilege was lost by disclosure to “third parties”, which in this instance consisted of the company’s chairman of the board of directors, the directors, the financial controller and the two external auditors of the company.

For the purpose of legal professional privilege, neither the financial controller nor the two external auditors were to be considered “third parties” but as insiders who would ordinarily be concerned with the allegations in the legal opinion.

The Federal Court held that the finding of the Court of Appeal that privilege was lost or could not be claimed because the legal opinion was already in the hands of the opposite party was unsustainable. Where legal professional privilege is invoked, the rule is one of admissibility of the document. A document is inadmissible if it is privileged, even if the other party has possession.

(iv) *Discovery under O.24 of the RHC*

In the pre-trial discovery proceedings, the GM disclosed the legal opinion in Part 1 of Schedule 1 of his list of documents. The plaintiffs contended that by doing so, he had chosen to waive the privilege attached.

The Federal Court held that the mere placement of the privileged document in Part 1 is not fatal and does not amount to a waiver of privilege. While the GM had placed the legal opinion under Part 1 of Schedule 1, there was a rider claiming legal privilege at para 2. This was sufficient as it complied with O.24 r.5(2) of the RHC.

The Federal Court held that the Court of Appeal’s finding that the GM had “expressly consented” to production of the legal opinion disregarded the specific objection he had raised. Order 24 provides a right of inspection of documents disclosed in the list of documents and cannot be taken as overriding the substantive legal provisions governing privilege contained in s.126 of the Act.

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Legislative Update

Income Tax (Amendment) Act 2009 [Act A1349]

The Income Tax (Amendment) Act 2009 (“the Act”) was gazetted on 23 April 2009. It incorporates some of the tax incentives announced in the second stimulus package to Budget 2009.

Among the significant tax incentives contained in the Act are:

- (a) In determining their taxable income, individual tax residents may deduct the interest expended to finance the purchase of a residential property. This is provided the property is purchased between 10 March 2009 and 31 December 2010 and the taxpayer does not derive any income from the property; and
- (b) Some part of the compensation received by a taxpayer for loss of employment is exempted from income tax. The amount exempted from income tax is limited to RM10,000 multiplied with each year of service with the employer.

The following Acts were gazetted on 8 January 2009:

- (i) Finance Act 2009 [Act 693]
- (ii) Malaysian Anti-Corruption Commission Act 2009 [Act 694]
- (iii) Judicial Appointments Commission Act 2009 [Act 695]

(i) Finance Act 2009

The Finance Act 2009 seeks to amend the Income Tax Act 1967, among others. As outlined in Chapter II, the Finance Act 2009 introduced eight new sections.

Among them are s.15B (derivation of gains or profits in certain cases), s.77B (amendment of return), s.97A (notification of non-chargeability) and s.109F (deduction of tax from gains or profits in certain cases derived from Malaysia).

The dates and years of assessment for which the changes are to take effect are contained in s.3.

(ii) Malaysian Anti-Corruption Commission Act 2009

The objectives of this Act, as enumerated in s.2, are:

- (a) to promote the integrity and accountability of public and private sector administration by constituting an independent and accountable anti-corruption body; and
- (b) to educate public authorities, public officials and members of the public about corruption and its detrimental effects on public and private sector administration and on the community.

It came into force on 1 January 2009.

(iii) Judicial Appointments Commission Act 2009

This Act provides for the establishment of the Judicial Appointments Commission and applies to the appointment of judges of the Federal Court, Court of Appeal and High Court and judicial commissioners, including the appointments of the Chief Justice of the Federal Court, the President of the Court of Appeal, the Chief Judge of the High Court in Malaya and the Chief Judge of the High Court in Sabah and Sarawak made on or after 2 February 2009.

Apart from setting out the functions and powers of the Judicial Appointments Commission (see s.21), the Act mandates the prime minister to uphold the continued independence of the judiciary (s.2).

It came into operation on 2 February 2009 by order published under PU(B) 43/2009.

In May 2009, the Minister of Finance made the following order and regulations, which took effect on 1 January 2009.

Insurance (Exemption) (No 3) Order 2009
[PU(A) 185/2009]

This order made pursuant to s.198 of the Insurance Act 1996 [Act 553] exempts a licensed insurer from requirements outlined in these sections of that Act:

- s.46 (margin of solvency);
- s.50 (security for credit facility);
- s.51 (valuation of security);
- s.58 (notification of non-compliance with margin of solvency);
- s.59(1)(a)(iii) (action against insurer, employee or director); and
- s.93(b) (restriction on payment of dividend).

Insurance (Amendment) Regulations 2009
[PU(A) 186/2009]

Amendments to the Insurance Regulations 1996 [PU(A) 653/1996] made pursuant to s.202 of the Insurance Act 1996 mainly affected the following:

- regulation 11 (surplus for participating policies);
- regulation 69 (surrender value disclosure to proposer);
- regulation 71 (surrender value);
- regulation 72 (surrender value for policies issued on or before 31 December 2008);
- regulation 73 (variation of basis for surrender value);
- regulation 75 (paid-up policy); and
- regulation 76 (variation of basis for paid-up value).

At the same time, regulations 68 and 70, Parts VI to IX, XI and XIII, as well as the First Schedule were deleted.

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SC adds to Islamic securities list

In late May, the Securities Commission (“the SC”) released an updated list of 848 Islamic securities across different sectors approved by its Shariah Advisory Council (“the SAC”). The securities constitute 88% of the listed securities on Bursa Malaysia.

The capital market regulator’s revised list approves 13 newly classified securities, among which are builder Sunway Holdings Bhd, paper box maker Box-Pak (Malaysia) Bhd, and developers Daiman Development Bhd and I-Berhad. But leisure company Reliance Pacific Bhd, which had been in the list issued in November 2008, was dropped.

Shariah-compliant securities include ordinary shares, warrants and transferable subscription rights. Warrants and transferable subscription rights are classified as Shariah compliant if the underlying shares are also Islamic. Loan stocks and bonds are deemed non-Shariah compliant securities unless they are issued based on Shariah principles.

Where the activities of a company listed on the Malaysian bourse are concerned, the SAC uses a standard criterion. If the activities are not contrary to Shariah principles, the company will generally be classified as Shariah compliant. Non-Shariah compliant core activities range from the provision of financial services based on *riba* (interest) and stockbroking in non-Islamic securities to the manufacture or sale of non-halal or tobacco-based products.

The SAC also considers the level of contribution to the company’s income of interest from conventional fixed deposits or other interest bearing financial instruments, as well as dividends from investing in non-Islamic securities.

If the activities comprise both permissible and non-permissible elements, the company is subjected to two additional criteria:

- (a) public perception of the company or its image must be good; and
- (b) the core activities are considered *maslahah* (beneficial) to Muslims and the country, and the non-permissible element is small and involves matters such as *`umum balwa* (common plight and difficult to avoid), *`uruf* (custom) and the rights of the non-Muslim community which are accepted by Islam.

Other details on classification and the SAC’s guidelines on the disposal of non-Shariah compliant securities are in the list, which is available from the SC website at www.sc.com.my/eng/html/icm/sas/sc_syariahcompliant.pdf.

The revision is part of a regular exercise that takes place twice a year. The next update is in November.

Free copies of the list in booklet form are being made available from 16 June 2009. **LH-AG**

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Sowing the SEED of knowledge

Following on the second stimulus package announced in March 2009 by the Malaysian government, one of the main thrusts of which is reducing unemployment and increasing job opportunities for Malaysians, the Securities Commission (“the SC”) launched its Executive Enhancement and Development programme, called “SEED”, for young graduates eyeing a career in the capital markets industry.

The new initiative, which was rolled out in late May, seeks to provide 500 of them with training and on-the-job attachment to enhance their employability and career mobility in this segment of the finance industry.

The SEED programme is essentially made up of three training schemes designed to create entry-level professionals for the conventional and Islamic capital markets, as well as executives for various regulatory functions within the SC and Bursa Malaysia.

The schemes, which will adopt the approach of structured learning for knowledge acquisition and experiential learning for skills acquisition, such as interpersonal development, include on-the-job stints of 11 to 22 months with capital market intermediaries.

Participants will also be eligible to sit for the SC’s licensing examinations, thereby helping to lower training and development costs of new entrants for the intermediaries, in addition to providing a ready pool of “fit-for-purpose” graduates for recruitment in the capital market.

The Shariah component of the SEED programme, called the Islamic Capital Market Graduate Training Scheme (ICMGTS), will begin on 1 July 2009. Details on the criteria and the programme brochure are available at the Securities Industry Development Corporation (SIDC) website at www.sidc.com.my/programme/icmgts.html. SIDC is the training and development arm of the SC.

The SEED programme is funded by the SC and the Capital Market Development Fund. **LH-AG**

For the speech by SC chairman Dato’ Sri Zarinah Anwar at the launch of the SEED programme, see www.sc.com.my/main.asp?pageid=375&linkid=2153&yearno=2009&mod=paper

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